

INDIAN ECONOMICS

*Being a Comprehensive and Critical Survey of the
Economic Problems of India*

VOL. II

BY

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BOMBAY

D. B. TARAPOREVALA SONS & Co.

Kitab Mahal, 190, Hornby Road

1929.

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CHAPTER I

Industrialisation : Means and Methods

§ 1. The position regarding industrialisation restated :—The desirability of a varied industrial development in India may be taken as established on economic as well as important non-economic grounds.* It has been repeatedly pointed out that so long as the country retains her overwhelmingly agrarian character and so long as the salient feature of India's international trade remains the exchange of raw materials for manufactured articles imported from abroad, the position must be regarded as highly unsatisfactory from the national point of view. To plead for industrialisation is not to forget the importance of agricultural development in this country. For we have already seen that the most rapid industrial progress conceivable under the present circumstances in India will for a long time leave agriculture occupying a predominant position in the life of the Indian people. And we have written in vain if we have failed to impress on the reader the necessity of directing strenuous effort towards improving the practice and organisation of agriculture in India. At the same time, however, for reasons already adverted to and even in the interest of agriculture itself, † the development of modern industries, as rapid as wisely applied private and public effort can make it, is a consummation devoutly to be wished.

PROTECTION.

§ 2. Protection as a help towards industrialisation:—The people in this country have always looked to the state for leading the nation into new paths and the extreme form of individualistic philosophy, which once dominated popular thought in England and which regarded all state interference as "mere vanity and vexation of spirit," never had any considerable following here. And it is all the less likely to gain adherents in this country

* See § 10, Chap XIII, Vol. I.

† See § 9, Chap XIII, Vol. I.

now that it stands largely discredited in England itself. The state will, therefore, be called upon actively to interest itself in the matter of industrialisation and take the initiative in devising and enforcing measures calculated to promote it. Among the various measures which it is expected to take, the first place is generally accorded to the establishment of a definitely protective tariff and, as previously mentioned, the Tariff Board is already busy working out the details of the policy of protection now formally accepted by Government.

§ 3. Free Trade and its limitations:—Although it is perfectly true that, under favourable conditions, Free Trade is calculated to secure (a) “the greatest mass of goods in the world as a whole, and (b) the greatest possible of immediate comfort for each consumer,”* it is now generally agreed that the Free Trade doctrine has its limitations and that, while laying stress on the well-being of the world as a whole, it rather tends to throw into the background the idea of the nation as a unit with interests often at variance with the interests of other nations. *A free exchange of goods and services between nations may be a good thing provided the different countries are at about the same stage of economic development*, but it may be positively harmful to economically backward countries preventing them from ever producing those commodities in respect of which they may have the greatest potential advantages. On this consideration rests in fact the well-known *Infant Industry argument for protection*. If the object of Free Trade is to ensure that every country should devote itself to those industries in which it has the greatest relative advantage, this object is not always fulfilled under untrammelled Free Trade. For, as John Stuart Mill pointed out, “the superiority of one country over another in a branch of production often arises only from having begun it sooner. There may be no inherent advantage on one part or disadvantage on the other but only a present superiority of acquired skill and experience. A country which has this skill and experience yet to acquire may in other respects be better adapted to the production than those which were earlier in the field.” But the mere fact that the latter had got an initial start and

* Cunningham: *The Free Trade Movement*, p. 9

are already in full possession of the field may act as an immense advantage. The other country may have superior natural facilities but having come later it may never be able to overtake the countries which had the benefit of an earlier start, or at any rate the process may take an unduly long time. Prof. Pigou has summed up the argument as follows:—"The main element of productive power, whose development involves a long process, is a population trained in the general atmosphere of industrial pursuits. If a country is entirely agricultural and has no important class of artisans or factory workers, the skill required for starting any particular kind of mill will be very difficult to get. 'Masters, foremen and workmen must first be either trained up at home or procured from abroad, and the profitableness of the business has not been sufficiently tested to give capitalists confidence in its success.' For a long time, therefore, it is improbable that any work which may be started will be able to compete on equal terms with established foreign rivals and that in spite of the fact that the industry in question may be one for which the country has great natural advantages. On the other hand, in a country which is already largely industrial, the initial difficulty involved in starting a new industry is likely to be much slighter. For, much less time is required to obtain from among a people already accustomed to many varieties of factory work, hands capable of carrying on a new variety of it. Further in an industrial community, those other important elements of productive power, organised systems of transport and of credit, which in an agricultural country may need themselves to be built up before manufactures can be profitably established, are presumably already in existence."†

As Prof. Coyajee points out, the argument for providing artificial props to young industries derives additional support when we remember that "the advantage always enjoyed by established enterprise has been greatly increased by the growth of massive production, the massive treatment of by-products, and by the internal and external economies corresponding to the expansion of business units and industries. Capital is needed on

† Quoted by the *Fiscal Commission's Report*, para 65.

an ever increasing scale to compete with large manufacturing establishments abroad " and may not be forthcoming all at once in the required quantities in an industrially undeveloped country. *The competitive power of fully established enterprises in foreign countries has been in recent times enormously increased* by the development of industrial combinations, trusts and monopolies. Owing to modern improvements in transport and low freights the natural handicap of foreign commodities is tending to be negligible. Lastly, the modern methods of competition which include dumping, export bounties etc., can sometimes be used with such deadly effect that resort to special measures of protection to infant industries becomes necessary.*

Several instances of successful application of the principle of protection to infant industries can be quoted. The iron industry in the U. S. A., for instance, would certainly not have made such rapid progress but for the stimulus of protection in its childhood. It is worth while quoting the following words of Prof. Taussig in this connection :—"It might be alleged that the iron industry would have advanced during the forty years in much the same way, protection or no protection. And yet the unbiassed enquirer must hesitate before committing himself to such an unqualified statement. Rich natural resources, business skill, improvements in transportation, widespread training in applied science, abundant and manageable labour supply—these, perhaps, suffice to account for the phenomenon. But would these forces have turned *in this direction* so strongly and unerringly but for the shelter from foreign competition? Beyond question, the protective system caused high profits to be reaped and the stimulus from great gains promoted the unhesitating investment of capital on a large scale....Thereafter the community began to get its dividend. Prices fell....The same sort of growth would doubtless have taken place eventually, tariff or no tariff; but not so soon, or on so great a scale.

No one can say, with certainty, what would have been; and the bias of the individual observer will have an effect on his estimate of probabilities. The Free Trader...will be slow to admit

* See J. C. Coyajee: *The Indian Fiscal Problem*, p. 4

that there are any kernels of truth under all this chaff....On the other hand, the firm protectionist will find in the history of the iron trade exclusive proof of brilliant success. And very possibly those economists who, *being in principle neither protectionists nor free traders*, seek to be guided only by the outcome in the ascertained facts of concrete industry, would render a verdict here not unfavourable to the policy of fostering "national industry."*

§ 4. The main argument for Protection in India:—It is not necessary for our purpose to recapitulate all the usual arguments for protection. We are concerned only with those which have figured with any degree of prominence in the controversy as carried on with reference to India and our apology for dealing at some length with *the Infant Industry argument* is that it is commonly accepted as the strongest argument favouring the introduction of a system of Protection in this country. It is taken for granted that under Protection a large number of industries will spring into life and that if they are assured of reasonable profits during the early years of development, they will rapidly grow in strength and efficiency so that they will be able eventually to dispense with all artificial aid, and the loss entailed during the the initial stages of development will be more than covered by the ultimate advantage to the nation. We have already given reasons for holding that the potentialities of this country for evolving industries of the modern type are very considerable† and the opinion so widely held in India that Protection would be a powerful, not to say an indispensable, aid to the realisation of these potentialities has been supported in unmistakeable terms by the Fiscal Commission, which quotes with approval the following words of Prof. Pigou pointing out their obvious applicability to India:—"The case for Protection with a view to building up productive power is strong in any agricultural country which seems to possess natural advantages for manufacturing. In such a country the immediate loss arising from the check to the exchange of native produce for foreign manufactures may well be outweighed by the gain from the greater rapidity with which the home manu-

* Taussig : *Some Aspects of the Tariff Question*, B. K. IV, Chap II, p. 29.

† See § 7, Chap, XIII, Vol. I.

facturing power is developed. The 'crutches to teach the new manufactures to walk,' as Colbert called protective duties, may teach them this so much earlier than they would have learnt it, if left to themselves, that the cost of the crutches is more than repaid. **

§ 5. Protection and diversification of industry:—The development of a varied type of industry is in itself a desirable goal as affording a field for the employment of different grades of skill and as having a salutary influence on the national character, and in so far as Protection leads to such development we have another argument in its favour. It would, however, seem *needless for this country to undergo any special sacrifice for the express object of securing a sufficient diversification of industries*, as this object will be incidentally fulfilled even if protection is extended only to those industries which will eventually be able to discard it. It is the conviction of most people who advocate protection for India that a large number of industries will spring up and thrive under it, and will be in a position to face world competition after the lapse of a brief period of artificial support derived from a protective tariff.

§ 6. Protection and National Self-sufficiency:—Protection is sometimes advocated on the ground that it can be used for making a country economically self-sufficient. It may, however, be pointed out that *those who are in favour of protection are also for encouraging exports by every possible means. But this is clearly incompatible with the ideal of self-sufficiency as imports must increase pari passu with exports.* Apart from this consideration, it may be questioned whether national self-sufficiency is any more desirable as an ideal than individual self-sufficiency. As Prof. Cannan remarks, "The superlative protectionist is the hermit who declines to buy anything from his neighbours." § And a *hermit nation is no more worthy of admiration than a hermit individual.* A nation which refuses to buy anything from other nations must either produce itself all that it needs or must go without some things which add to its well-being; in

* Fiscal Commission's Report, para 74.

§ See The Economic Journal, March 1919, page 79.

either case there will be a loss in terms of welfare. *Generally speaking, the ideal of self-sufficiency should be pursued only within the limits set by the principle of comparative cost*—which in the present context is merely another way of saying that, as a general rule, protection should be thought of only in connection with those industries in which a country possesses undoubted natural advantages.

The doctrine of national self-sufficiency is often supported from the standpoint of national defence. National safety, it is argued, requires that a country should aim at economic independence—even if this should entail a permanent burden on the community. There are, however, definite limits to the practical application of this maxim. *It may be feasible and desirable to sacrifice economic considerations and to nurse a few industries for the avowed purpose of national defence. It would, however, be sheer folly to try to regulate normal peace economy on a war basis.* The United Kingdom, for example, cannot think of raising all the food required for her population, because in the event of a war with a first-rate power her supplies coming from abroad may be cut off by an effective food-blockade. She would clearly benefit most by the widest extension of her overseas commerce combined with the possible adoption of all necessary measures for maintaining her supremacy at sea in order to prevent a blockade. The fact that India is a country possessing varied resources brings self-sufficiency within the bounds of practicability for her than in the case of any more country like England. She need not, for example, depend on foreign countries for her food-supplies. But it is neither possible nor desirable that she should be completely independent of other countries for the satisfaction of *all* her wants. Evident of other military requisites, not all of them can be produced in the country itself and some of them cannot be produced except at a sacrifice which on the whole is not worth while. The principle of protecting an industry on the ground that it is essential for the purpose of national defence is valid enough in a general case it will be necessary to weigh the military value of the industry against the economic sacrifice required for maintaining it and, as the Fiscal Commission remark, “the decision must be based on a sense of proportion.”*

* See F. C. Report, 107.

§ 7. The case of basic industries :—Basic Industries or “ key industries ” i. e. industries whose products are utilised as raw materials, on an assured supply of which the prosperity of a large number of important industries depends, have already been recognised as deserving special consideration and the British Safeguarding of Industries Act has admitted the principle of protecting them. The work of selecting industries for protection on this ground requires particular care and vigilance, for almost every industry will demand protection on the plea that it is in some sense or other a basic industry and may get it without any rational justification for such special treatment. For example, there are already loud complaints in England that the interests of the consumers have been needlessly and recklessly sacrificed in this manner by an indiscriminate application of the safeguarding principle.†

§ 8. Protection and Public Revenue:—Apart from rapid industrial development other advantages are also claimed for Protection. It is said, for example, that protection will have a salutary effect on the public revenues. To say the least, however, this consequence is of a highly problematical character. If, before levying protective duties certain commodities were being admitted free of duty, it is obvious that so far the income from customs duties will increase. On the other hand, however, the inevitable rise in prices will decrease the taxable capacity of the consumers. If it is a case of raising an existing duty on the imported article for purposes of protection, the effect on the revenue will depend on the quantity that continues to be imported in spite of the higher duty. If the protection afforded by the duty is really effective the imports ought to contract rapidly with corresponding diminution of revenue. It is conceivable that a very

† “Among the articles scheduled as necessary to the safety of the country by the pundits of the Board of Trade were included toy magic-lanterns, soothing syrups, glass berries for millinery, toy magnets for the fishpond game, and howlery latch needles.” F. W. Hirst, *Safeguarding and Protection*, p. 39.

§ The rise in prices will not be limited to the protected commodities but will generally extend to other commodities as well by “sympathetic” action, locally produced substitutes for the imported articles being the first to be affected by the rise in price of the latter. F.C. Report, pp. 43-44.

high import duty even with a greatly reduced volume of imports should happen to be most satisfactory from the revenue point of view, but this result cannot be counted upon. In any case, it would be always necessary to make some deduction on account of the smaller taxable capacity of the consumers. It is further conceivable that Protection by concentrating wealth in the hands of a small number of people engaged in the favoured industries, may, for example, increase the yield of direct taxes like the incomes tax (with its usual accompaniments of exemption of minimum income and progression); the larger yield from the higher incomes may outweigh the reduced yield from the taxes on the smaller incomes, direct as well as indirect. The net result of Protection on revenue depends on so many complex factors that it is impossible to predict with confidence whether the revenue will gain or lose.

These considerations apply to short-period results. If, however, we take a sufficiently long period for the protective duties to work out their full effects and if we assume that they have been wisely levied, the public revenue ought certainly to benefit in the long run from the enrichment of the country and the greater taxable capacity of the people. *But we must keep the short-period and long-period effects separate and a country entering upon a protectionist regime ought to be prepared for difficulties in connection with balancing its budget.*

§ 9. Protection via Revenue Duties :—The Fiscal Commission Report lends countenance to the view that Protection was anyhow inevitable in this country because the enormous increase of public expenditure since the War had already compelled Government very greatly to increase duties on imports—a procedure which was unintentionally protective as regards many manufactures. Such protection being “casual and haphazard” was bound to carry with it certain undesirable consequences. It gave protection without any assurance of a permanent policy and not necessarily to industries which deserved it. High customs duties intended for revenue but accidentally protective may, far from accelerating India’s development, actually hinder it very seriously, e. g., by taxing raw materials and semi-manufactured

articles. A situation of this type, according to the Commissioners must inevitably lead a country into the path of conscious and deliberate protection.

This line of reasoning seems to suggest that, under certain circumstances such as those detailed above, a country may be forced into Protection although conditions commonly supposed to justify it may be absent. It is a fact that Government in this country had to meet their financial difficulties by resorting, to an unprecedented extent, to import duties and that probably it was not practicable to offset them by countervailing excise duties in every case. These difficulties may perhaps be said to have hastened the advent of protectionism proper for which, however, *a clear and independent case* had to be made out before it could be introduced. It was not adopted and it would have been wrong if it had been adopted as a kind of *pis aller*. *Protection was introduced for the positive benefits expected from it and not merely as an escape from a system of unintentionally protective revenue duties.* This criticism may seem hyper-critical, but the way in which the Commissioners state the matter tends to obscure the fact that *the revenue and protective aspects of the tariff are essentially mutually irreconcilable and ought to be kept separate as far as possible.* If both the objects of revenue and protection are well served simultaneously by an identical set of duties, this can only happen by accident and as a rule only temporarily.

§ 10. Strong Sentiment for Protection in India :—Opinion in India has been for a long time preponderatingly in favour of Protection and the pressure of public opinion has in a large measure dictated the actual introduction of a deliberately protective tariff. If Protection was a mistake, it was felt that it was better to let the Indian people find this out for themselves by actual experience instead of forcing them to keep free from the fetters of Protectionism. The policy of Free Trade for India was all the more obnoxious to the people owing to *the suspicion that the open door in India was favoured by England in her own interests and not so much in India's interests*, a suspicion not altogether groundless. The way in which Lancashire was allowed to meddle with fiscal and industrial policy in this country from time to time strengthened this attitude of distrust. Further, *the*

memories of by-gone days, when India was renowned for her manufactures, added poignancy to the natural regret felt by patriotic Indians contemplating her present insignificant position as an industrial nation, which seemed to them to be the prime cause of India's poverty. *Other countries like the United States, Germany, and above all Japan appeared to have prospered exceedingly under and because of Protection*; and arguments, however plausible, trying to show that their prosperity was mainly due to quite other causes and that Protection was rather an impediment than a help to their industrial development failed to carry any conviction, especially as they were urged mostly by Englishmen whose bonafides were not accepted. It was pointed out that England herself had discarded Protection only when her pre-eminence in industry had been securely established and that anyhow the beginnings of the Free Trade regime in England aimed at *assisting industry* by withdrawing advantages from agriculture which were harmful to manufactures.

Lastly, in recent years, *England herself has been steadily drifting into a policy of Protection*. In 1915, the McKenna Duties made the first real breach in the traditional system of Free Trade and under the Safeguarding of Industries Act of 1925 protection has been granted to a number of industries and the use of the euphemistic word "Safeguarding" instead of the more honest word "Protection" has not deceived anybody as to the nature of the change. It is clear to everyone that England's fiscal policy at present has not only ceased to "sound in tune with the verbal jingle of an abstract dogma" (i. e. the Free Trade dogma) but amounts to a definite abandonment of Free Trade, and under the circumstances it does not lie in the mouth of England to preach Free Trade to India. It is, however, only fair to mention that although a few economists of note in England have always denounced the unrestrained pursuit of cheapness and characterised it as "atomism and premature cosmopolitanism", the trend of expert opinion is still on the whole strongly against Protection, as also the opinion of many powerful business interests which have thriven greatly under Free Trade.*

* For example, Lord Inchcape speaking on the Merchandise Marks Act of 1926 said, "Under Free Trade the country has prospered for the last

§ 11 The cost of Protection:—It must be noted that much of the popular enthusiasm for Protection is due to the failure to recognise clearly the disadvantages and dangers of a protectionist policy as well as an exaggerated notion of what it can achieve by itself in the way of economic revival. The doctrine of Protection possesses a certain persuasive plausibility and its appeal is instant to the man in the street not accustomed to economic analysis. In order, however, that Protection should be used to the best advantage, it is necessary to have a clear idea of the various kinds of sacrifice it involves and an intelligent attempt must be made to minimise the sacrifice. In the first place, *Protection will necessarily increase the cost of living. The consumers as well as those industries which are not protected will suffer owing to increase of expenses.* The burden imposed on unprotected industries is commonly ignored and that is one of the reasons why Protection finds ready adherents amongst the uninstructed public. As a certain writer puts it, "For every *plus* there must be a *minus*; perhaps people are protectionists merely because it is generally easier to see one plus than a multitude of *minuses*."†

Wages will rise with the cost of living but generally they do not rise as fast as prices. Although *the skilled labourer*, especially in the protected industry will benefit, *the unskilled labourer*, on account of his excessive numbers, will probably be worse off as the result of Protection. The wages of the *agricultural labourer* may also rise, particularly in the neighbourhood of industrial

century beyond all bounds. I am getting on in years, and if the catastrophe of Protection comes, it may not come in my time; but I venture to say that in my humble judgment if the Government interfere with the free exchange of commodities between this country and the world, Great Britain will become a mere cypher. Unemployment will increase, taxation.....will wipe out the country's wealth, and these little islands in the North Sea will sink to a place of no importance in the world...We are not a self-contained country and we never shall be unless our population diminishes by three-fourths of what it is at present. We live by what we manufacture and send abroad and by the ships we build, and these are paid for by international trade'. Quoted by F. W. Hirst, *Safeguarding and Protection*, pp.95-96.

†C. H. Oldham's article on *Industrial Ireland under Free Trade* in the *Economic Journal*, June 1917.

centres, but it is doubtful whether they will quite overtake the increased cost of living. As regards *the agriculturist who owns the land which he cultivates*, his expenses will be greater owing to the higher wages of any outside labour he may employ and he will also have to pay higher prices for his implements. On the other hand, he will get more for the produce he sells.* But if he has not much surplus to sell he will lose by Protection. *The middle classes* will undoubtedly be the losers under a protective system, for it may be taken as almost certain that their incomes will not rise in proportion to the increase in prices. The middle classes, however, have been the strongest supporters of Protection in this country. To some extent, no doubt, this is because their education and enlightenment enable them to take a broad national view of Protection which they welcome in the interests of industrial advancement and are prepared cheerfully to face the harder life which it must mean to them as a class. But, as suggested above, the enthusiasm for Protection is largely the product of ignorance and incapacity vividly to realise its inconveniences. When Protection has been in actual operation for some time and produces the expected consequence of enhanced prices, it would be surprising if the present enthusiasm of the middle classes does not sensibly cool off.

§ 12. Discriminate Protection :—Most sections of the population, therefore, will have to go through a period of suffering and sacrifice in consequence of Protection and this is a serious consideration in a country where there is already far too much economic distress. The mistake must not be made of attributing to Protection the benefits which will have good reason for expecting from industrialisation and to which it is a means. *Protection is a purgatory through which the nation must pass before reaching the heaven of a well-developed industrialism.*† We may decide, as we have decided in the case of India, that the temporary suffering is

* There is, however, the possibility of a fall of prices of agricultural produce due to the curtailment of exports following curtailment of imports which Protection involves,

† We may appear to be somewhat lukewarm supporters of Protection for India but the fight for the principle of Protection having been won, we consider that an insistence on its dangers and the necessity of minimising them is now more to the purpose.

well worth while having regard to the highly desirable nature of the object to be achieved, but we must not suppose that Protection is a painless remedy for industrial backwardness. Being essentially an unpleasant remedy we must take care to use it only when on a balance of considerations the ultimate advantages appear clearly greater than the immediate disadvantages; we must also not use it in unduly large doses, that is to say, the rate of the protective duty should not be needlessly high; and lastly, we must stop its use as soon as it becomes unnecessary or in case it fails to show the good results anticipated from it. This is what is meant by "Discriminate Protection", which requires a most thorough and careful inquiry into the conditions of an industry before protection is extended to it.

Now that Government have definitely accepted the policy of Protection and will be pressed on all hands by all kinds of suitors asking for protection on every imaginable pretext † and they must have the courage to refuse protection to industries which fail to satisfy certain necessary tests. *Discriminate Protection* while giving the necessary stimulus to industrial development will minimise the burden on the community in various ways. In the first place, it *would restrict the rise of prices* to a minimum by refusing to grant wholesale protection to practically every industry that may ask for it. And secondly, it will *curtail the period of the burden* by preventing the diversion of labour and capital to unsuitable industries which will always require to be bolstered up at the expense of the community and by making the substitution of efficient methods for old-world inefficient ones a condition of admission to the benefits of protection. Besides shortening the period of the burden, *wise discrimination will further be in the best interests of the industries themselves*. High duties indiscriminately levied on imports will stimulate a host of weak and inefficient enterprises, the inevitable collapse of which

† "They tell in the United States, how a deputation of fruit-growers once waited on the President to appeal for a protective duty on bananas 'But, gentlemen,' he replied in astonishment, 'we do not grow bananas, where would the protection come in?' 'It is this way,' was the explanation, 'we are in the orange trade, and we feel that when a man is filled up with bananas he has no room for oranges.' If it be a myth, it is a luminous one." Robertson : *Trade and Tariffs*, p. 278

would shake the confidence of capital which is essential for steady industrial progress. They are also likely to unsettle labour which will be attracted from the sound to the unsound industries in the period of unhealthy boom caused by indiscriminate protection and which will be involved in the ruin sure to overtake them sooner or later.*

§ 13. Guiding principles of Discriminate Protection :—Certain general principles of Discriminate Protection as enunciated by the Fiscal Commission have been adopted for the guidance of the Tariff Board, to whom has been entrusted the onerous and delicate work of examining the fitness for protection of the various industries, recommending a suitable rate of protection, supervising the progress of the industries enjoying protection, and recommending its withdrawal as soon as it has done its work. The general conditions to be satisfied by industries before protection is granted have been stated as follows by the Fiscal Commission:—

(1) *“ The industry must be one possessing natural advantages, such as an abundant supply of raw materials, cheap power, a sufficient supply of labour, and a large home market. Such advantages will be of different relative importance in different industries, but they should all be weighed and their relative importance assessed. The successful industries of the world possess certain comparative advantages to which they owe their success. No industry which does not possess some comparative advantages will be able to compete with them on equal terms, and therefore the natural advantages possessed by an Indian industry should be analysed carefully, in order to ensure as far as possible that no industry is protected which will become a permanent burden on the community.*

(2) *The industry must be one which without the help of protection either is not likely to develop at all or is not likely to develop so rapidly as is desirable in the interests of the country. This is an obvious corollary from the principles which have led us to recommend protection. The main object of protection is either to develop industries which otherwise would not be developed or to develop them with greater rapidity.*

* F. C. Report, pp. 49–50.

(3) *The industry must be one which will eventually be able to face world competition without protection. In forming an estimate of the probabilities of this condition being fulfilled the natural advantages referred to in condition (1) will of course be considered carefully. The importance of this condition is obvious. The protection we contemplate is a temporary protection to be given to industries which will eventually be able to stand alone.* '*

Other subsidiary suggestions are that industries subject to the law of increasing returns as well as those which promise before long to satisfy the entire needs of the country should generally be regarded as fit subjects for protection. On the other hand, as a general rule an industry which can never meet more than an insignificant proportion of the home demand should not receive protection. Protection to one industry may possibly injure another; but protection should not necessarily be refused to an industry on this ground for there may be a net advantage on the whole in protecting it, and like consumers the producers also must sometimes be prepared to sacrifice their interests when a policy framed in the general interests of the country requires it.

Protection may sometimes have to be resorted to or increased as a measure against certain forms which modern international competition takes. One of these is described as '*dumping*' which is said to occur when goods are sold to the foreign consumer at a lower price than in the country of production. Where the producer has a practical monopoly of the home market, he may find it on the whole profitable to charge fairly heavy prices to the home consumer and dispose of the surplus in the foreign market at substantially reduced prices. If this practice is not merely temporary there does not seem to be any reason why the countries which get the benefit of the lower prices should complain. † But there is another kind of dumping which is more serious. It is resorted to as a temporary expedient and prices are quoted which if continued for a long time would prove ruinous to the producers, the intention here being to drive out of competition rivals in the country subjected to

* See F. C. Report p p. 54-55.

† See Edgeworth: *Papers relating to Political Economy*, pp. 119-120, Vol III.

the process of dumping and to recoup the lossess by charging higher prices when competition is thus extinguished. Such a method of eliminating competition can be adopted only if the dumper is virtually in command of the market of the world, for otherwise if there are other competitors in the field he will never be able to enhance the prices at will and thus reward himself for the heavy sacrifice he has undergone by selling at very low prices for some time. *When, however, dumping is clearly proved and it is injurious to some industry in the country whose prosperity is a matter of national concern, a special dumping duty may be necessary.* Similar action may be justified against the goods of a country whose currency is seriously depreciated enabling it to export them at prices which are excessively low in terms of a stable foreign currency. Lastly, *bounty-fed articles* coming from abroad may necessitate special measures of protection and there is already legal provision in this country for dealing with such a contingency. Act XIV of 1899 provides that "where any country pays directly or indirectly any bounty upon export, the Governor-General-in-Council may by notification in the Gazette of India impose an additional duty on importation into India equal to the net amount of such bounty". ‡

In the opinion of the Fiscal Commission the industries that will be found to satisfy the tests laid down for protection will be generally young industries. They recognise, however, that occasionally cases may arise where protection even to a strong and well-developed industry may be justifiable so as to enable it to recover from temporary depression due to causes beyond its control. No universal and dogmatic rule can, therefore, be laid down as regards the stage of development at which protection should be applied.

‡F.C. Report, p 81 The test to be applied in most of these cases is whether the lower prices of the foreign articles are likely to be permanent or temporary. If they are expected to be temporary there is a case for protection in view of the economic dislocation caused by sudden price movements.

In the case of *absolutely new industries*, however, the Commissioners think that it would be running too great a risk to grant protection relying on "the anticipations of the promoters" of the new venture rather than on actual facts. But even in dealing with existing industries, it will not be possible to avoid the traffic in anticipations and uncertainties altogether. What the Tariff Board will have to consider is the anticipation of the applicants for protection that with its help their industry would prosper and be able ultimately to stand on its own legs. No doubt the industry being already established there will be some solid facts to go upon making the forecast about its future course less speculative. The speculative element would be greater when it is proposed to extend protection to an industry in order that it may develop some new branch. The Commissioners do not look with disfavour on the policy of protecting an industry on this ground.* It is thus clear that the *element of speculation will always be present in a greater or less degree in every case where protection is demanded*. It may happen, however, that the element of uncertainty may not be too great even in an absolutely new industry. Reliable data may be available in other countries where it has been securely established and they may be of such a character as to leave no reasonable doubt about its success here under the temporary stimulus of protection or initial assistance in some other form. The Fiscal Commission thinks that generally in the case of new industries protection would not only be objectionable but unnecessary, as the financial necessities of Government will compel the retention of a general level of fairly high revenue duties and this will give all the protection that is necessary at the start. But this rather underrates the difficulties of making a start and loses sight of the fact that, in some cases, the beginnings may present far greater difficulties than the later stages of development and may require assurance of substantial help from the State before an industry otherwise promising can be started at all. The principle of Government assisting new ventures by providing the necessary guarantees for a bank granting accommodation † which has been favourably received in

* See F. C. Report, p. 56.

† See p. 484 above, Vol I.

most quarters is not essentially different from the principle of giving consideration to them with a view to protection. The main question involved in each case is whether the industry satisfies the general conditions laid down above. The first point to decide is whether an industry deserves special assistance and here the proposition that new industries because they are new should not generally be assisted is not likely to be very helpful.* The second point is to decide the form in which assistance is to be given, and sometimes bounties rather than import duties may be found more suitable. The Fiscal Commission's suggestion seems sound that *bounties should be the rule rather than a protective tariff in the case of new industries* because so long as an industry is not supplying any considerable proportion of the total needs of the country a protective duty will entail a disproportionately heavy burden on the consumer.

After it is decided to grant protection to an industry the next important question is to settle the *rate of protection*. Too heavy a rate would be wasteful and demoralising. The industry should not be protected so thoroughly that it ceases to exert itself any further. *What is really wanted is a stimulant and not an opiate.*

The test of fixing upon a rate of duty that is adequate without being excessive is one of the most difficult and in this connection the *question of relative costs* will demand careful consideration. It will be necessary to make sure that the relatively higher costs in India are not wholly due to inefficiency or other preventable causes. Again, for comparing the costs of production in India and foreign countries average representative firms will have to be taken and not more than ordinarily efficient or more than ordinarily inefficient firms.* The rate of protection must also be considered in relation to the *convenience of the consumer*. A high rate may have the advantage of bringing about a rapid development, but it may have to be low in the interests of the consumer and a comparatively slow development may have to be accepted as the lesser evil.

* To get an idea of the complexity of cost-analysis the reader should refer to Coyajee's *The Indian Fiscal Problem*, pp. 36-37.

§ 14. Dangers of Protection :—The Fiscal Commission refer approvingly to the Hon'ble Lala Harkishen Lal's maxim, "Nurse the baby, protect the child and free the adult" as a good summary of the correct principles of protection. The last part of this dictum, viz., the freeing of the adult presents one of the toughest problems of protection, because the adult is apt to kick and otherwise make himself unpleasant if an attempt is made to free him from his protectionist fetters which he finds very comfortable on the whole. When an industry comes under protection, it will naturally try to retain the advantage as long as possible and one of the methods it may adopt is to disguise its prosperity and make a show of infantine helplessness. But the danger in this is that it may be taken at its word and protection may be withdrawn on the ground that the industry has not derived any benefit from it. The other method is to bring political influence to bear upon the authority invested with the power of lessening or withdrawing the duty. To fix a definite period for protection at the time of granting it is not practicable and does not point to a way out of the difficulty.* It would be impossible to state the precise number of years that protection would be necessary in any given case because the conditions affecting the industry cannot be counted upon to remain unchanged. If conditions are fundamentally changed it will be necessary to reconsider the position and possibly extend the period of protection.

The Fiscal Commission express the view that the only way of maintaining a satisfactory control over a protected industry is for the Tariff Board to review periodically the position of the protected industry and make reasoned recommendations as to whether the duty should be continued or withdrawn and, if continued, whether the rate should be modified.

To perform this task effectively and without prejudice or favour requires rare intellectual and moral qualities besides a thorough knowledge of economic theory and facts. It is, therefore, necessary to choose the personnel of the Tariff Board with the greatest possible care. The success of the protectionist experiment depends on the manner in which this body works, for

* See F. C. Report, p. 67.

the Tariff Board has been erected into a kind of *deus ex machina* which is expected to solve every difficulty that will arise in giving practical effect to the policy of protection.

As previously stated, the Board has already considered a number of applications for protection and the manner in which it has disposed of them has served to give satisfaction and confidence to the public. It is, however, too early to predict that it will succeed in saving the country from the more serious evils associated with Protection. Its difficulties will have really begun when powerful vested interests arise under the shelter of a protective tariff and seek to manipulate it, as is their wont, in their own selfish interests and to the prejudice of the country in general. The experience of this and other countries shows that a competent and honest judiciary can be obtained if serious attention is given to the matter, and if a pure judiciary can be secured, there is no reason to despair of securing a competent and incorruptible Tariff Board. But it is a more difficult matter to secure a Legislature and a Government not liable to be influenced by particular interests in shaping the tariff policy of the country. It must be admitted that in most countries which have adopted Protection, tariff legislation is the resultant of the struggle of interested cliques and rarely follows a definite intelligent plan conceived in the interests of the country as a whole. † The Fiscal Commission, however, points out that the danger of political corruption is not so great in India as in some other countries on account of the variety of interests represented in the Legislature and the important position which the agricultural and landed interests will always occupy in the legislative bodies. This is perhaps taking an unduly optimistic view of the situation and underestimating the dangers of political corruption. The interests which prosper under protection will be able to command larger resources and better organisation than the interests opposed to them who would be too varied in character to combine effectively in the best way possible. At the same time all these dangers have to be faced

† "The history of tariffs in all countries shows that they represent far more the result of a conflict of interests than an impartial attempt to arrive at a policy in the interests of all." A. A. Mitchell in the *Economic Journal*, June 1925.

now that the plunge has been taken deliberately. The Fiscal Commission ¶ rightly emphasise *the necessity of the utmost publicity being given to the investigations by the Tariff Board* into the conditions of the industries soliciting special treatment. This would reduce the danger of corruption, provided the public is sufficiently instructed and vigilant. This consideration provides an additional reason for *spreading literacy and general enlightenment among the masses*. It would be highly desirable if the class of consumers whose interests are injured by Protection *should learn to organise themselves* into powerful associations and should see to it that Protection is kept within legitimate bounds and that their interests are not too recklessly sacrificed.

Besides political corruption *another evil to be guarded against is the development of combinations* of manufacturers which is stimulated by Protection. Here again it would fall to the Tariff Board to make sure whether a combination that may have arisen is actually injurious to the consumer's interests and if satisfied that such is the case, to recommend the diminution or withdrawal of protection by way of penalty.

§ 15. Protective Export Duties :—Something has already been said in another connection about the economic effects of restrictions on the free export of raw materials of industry, * and we have seen that export duties cause a disproportionate injury to the producer of raw materials without being of appreciable assistance to the manufacturers. The duties would have to be very high even to produce a comparatively small difference in the cost of the finished article in favour of the home manufacturer, as the cost of raw materials generally forms but a small part of the total cost of the manufactured article, † and the *hardship to the producer* will be so great as to make unthinkable the adoption of any general system of protection on this plan. Moreover, *if protection to a particular industry is necessary its burden should rest as far as possible on the shoulders of the whole community*. It is a wrong principle to penalise only one

¶ See F. C. Report, p. 47.

* See p. 224 above Vol I

† F. C. Report, p 108

particular class for the benefit of the protected industry. For this reason, as we have already suggested,* bounties and protective import duties are to be preferred to export duties. Another objection to export duties is that they carry with them the risk of a loss of the foreign market altogether as our bitter experience in the case of saltpetre has shown.†

§ 16. Other essentials than Protection:— India has adopted Protection inspite of its dangers and inconveniences as an essential aid to the speedy development of industries. We cannot, however, merely legislate a nation into wealth and prosperity and Protection alone will not achieve the economic transformation which is our goal. It will not convert the mediaeval organisation of a country into an up-to-date modern organisation as it were by the wand of a magician. ¶ *Even with protection a country may remain forever economically backward in the absence of an adequate development of indispensable adjuncts of modern economic life such as an efficient banking organisation, a properly developed system of transport, a sympathetic railway and shipping rates policy, an effective marketing organisation, an efficient system of commercial and industrial intelligence, adequate command of capital etc.*

Above every thing else what is required is *a change in the mental outlook* of all classes of people in India§ who must be

* See p 224 above Vol I

† See F. C. Report, pp. 104-105

¶ See Coyajee, op. cit, pp. 33-34

§ Dr. Marshall was no lover of Protection but he was a true friend of India. Being asked by an old pupil what he thought of Protection for India, this is what he wrote :—“ I have no objection on principle to the “Protection” of nascent Indian industries. But a customs tariff is an expensive method to this end : and under existing circumstances it would enrich European capitalists rather than Indian. Therefore, I think it should not be applied until other methods have been tried, not until those industries which already receive *a very high* protection from cost of carriage (in some cases double cost of carriage) have succeeded in evoking Indian enterprise. Strong cases in point I understand to be the leather, paper and oil-seed industries. If India had a score or two of men like Mr Tata, and some thousands of men with Japanese interest in realities, with virile contempt of mere speech-making in politics and law courts; and with no scorn for work

educated out of their present attitude of indifference, despair and helplessness and inspired with the vision of a great and powerful India which they must be prepared to strive hard and unremittedly to realise. The victory will not be gained in a day and the battle must be fought inch by inch and step by step. There will be many disappointments and progress may be slow. But if the nation is determined success is certain. We have too long been under the spell of the mischievous idea that poverty is inevitable and that wealth and industrial greatness comparable to those achieved by the foremost European nations is beyond the reach of India.

§ 17. Education:—The diffidence and lack of enterprise which characterise the Indian people today are defects largely attributable to the present faulty system of education which tends to turn out stunted ascetics rather than men at home in the practical work-a-day world and possessing the necessary knowledge and self-confidence born of a contact with reality on things while the mind was full of *thoughts*, India would soon be a great nation. Nothing could stop her: no tariff could hinder her: she would enter into her heritage. But so long as an Indian who has received a high education generally spends his time in cultured ease; or seeks money in Indian law suits—which are as barren of good to the country as the sand of the seashore—nothing can do her much good. So long as, with the exception of Bombay cotton—which after all is of Parsee origin—and a few works of which Mr. Tata's are at the head, all enterprise seems to be in European hands, in spite of the fact that the unhealthiness of India for the young children of Europeans is in effect a protective duty of perhaps 50-100 per cent in favour of Indian enterprise in India as against European. For twenty years I have been urging on Indians in Cambridge to say to others: "How few of us when we go to the West think of any other aim save that of our *individual culture*? Does not the Japanese nearly always ask himself in what way he can strengthen himself to do *good service to his country* on his return? Does he not seek real studies? Does he not watch the sources of Western power? Is not that the chief reason for Japan's quick progress? Can not we imitate her? Do we need any other change than, like the Japanese, to think of our country in the first place and ourselves a long-way behind?" *Memoirs of Alfred Marshall* edited by A. C. Pigou, p. 472.

For better or for worse (we think, on the whole, for better) India has made up her mind about Protection. None the less, Dr. Marshall's words deserve to be pondered over, for, Protection or no Protection, economic progress will be possible only in so far as the defects in national character to which Dr. Marshall points are remedied.

for improving their surroundings. It has long been a commonplace of educational discussions in this country that from top to bottom our educational system is too literary and academic, and that it is necessary to give a more practical bent to it. The ignorance and conversatism of the Indian peasant and the Indian labourer, industrial as well as agricultural, are proverbial. The considerations that we have already advanced in connection with the present unsatisfactory nature of the human factor in agriculture and the suggestions made for improving its efficiency hold good *mutatis mutandis* in the case of industrial labour as well.* The question of education is a question of life and death to modern nations and industrial efficiency must necessarily rest on a system of free compulsory education. The idea that all education creates a distaste for manual labour is erroneous. When a particular system of education is seen to produce this effect the remedy is to improve it, for a sensibly planned system far from creating a prejudice against manual labour ought to have a precisely opposite effect. Above all things it will emphasize the principle of the dignity of labour. One of the ideas in a sound scheme of education would be to make the scholar use his hands and eyes as much as possible, and subjects like drawing and manual training which are very valuable from this point of view must be included in the curriculum for primary education. Lack of any education or of education of the proper kind not only makes the Indian workman inefficient and unreliable but also kills in him all desire for improvement. Education will develop his wants, produce in him an incentive to work more and better in order to satisfy them and raise the whole tone of his life. One of the difficulties under which Indian industries labour is that skilled labourers as well as supervisors and foremen have often to be imported from abroad. The men thus imported are naturally expensive and they have to be given a high scale of wages and, in addition to this, heavy expenditure has to be incurred in connection with their repatriation. As we have already seen*, the suggestion has been made that foreign firms operating in this country should be required to train up a certain number of Indian

* See pp. 272-278 above, Vol. I.

apprentices. The Fiscal Commission recommend that Government should make the training of apprentices one of the conditions of the tender when they place important orders with foreign firms. Besides skilled labourers, supervisors and foremen, it is necessary to have Indian managers. The state technical scholarships abroad (about which more is said in the next section) can satisfy the need for the necessary training in this connection only to a very limited extent. The only real solution is to start technical institutes of all grades in the country itself so as to make it possible for Indian industries to dispense with foreign labour of every kind. Research in industrial problems is a function of the highest importance which the State alone can perform satisfactorily and the necessary institutions for this purpose must be created and maintained in the country at public expense. Among the greatest obstacles to industrial development in India must be counted the lack of enterprise and initiative among her businessmen. For industrial progress something more than mere technical knowledge is required. Men of insight, daring and organising ability are necessary to lead the country in the industrial march and to enable it to keep pace with other nations. The multiplication of Commercial Colleges is likely to help men of this type to discover themselves. The present deficiency in this regard is at least partially due to the fact that our educational system has not hitherto made it its special business to foster the qualities required for making a successful businessman. ‡ The excessively literary character of the education, which was originally intended merely to provide for the administrative needs of Government, has been in some measure miti-

‡The lack of industrial leadership has struck some observers as an insuperable obstacle to industrial progress in India and it is suggested that this is one more reason why India should concentrate on agriculture instead of industry for which her people are supposed to have no real aptitude. But improved agriculture on modern lines also requires the development of qualities in the people not dissimilar to those required for success in industrial pursuits. And if there are good reasons for the view that agricultural organisation on modern up-to-date lines is not an impossible ideal in India, neither is there any reason to despair of a similar development in the sphere of industries.

gated in recent years by the increasing importance being given to the teaching of modern science in our schools and Universities. The personal contact with specific realities and the exercise in verifiable reasoning which the laboratory makes possible has an obvious bearing on the thoughts and actions of men which are turned into useful practical channels. Commercial and technical schools and colleges ought also to have the same desirable effect. The increasing keenness of the struggle for existence is gradually forcing the educated classes to seek careers in business rather than in government service which cannot possibly provide for an unlimited number of graduates. There are reasons for expecting that the attractions of Government service and the overcrowded professions of law and medicine will diminish with the numerous openings that will come with the development of industries. All these changes are already perceptible but only just perceptible. They must proceed far more rapidly than at present and for this far greater efforts are necessary than are being put forth for improving and extending educational and industrial opportunities.

§ 18. The position of Industrial Education in India:—Though the facilities for industrial and technical education continue to be very meagre in the year of grace 1928, Government seem to have realised its necessity and importance as early as 1888, when a Resolution was issued on the subject calling upon the Provincial Governments to take action in the matter. The practical effect of this, however, was almost nil and for a long time the Victoria Jubilee Technical Institute, which had been started in 1887, chiefly through private efforts, in Bombay to provide courses of instruction suitable to the needs of the growing Bombay Mill Industry, was the only institute of its kind in the country. The investigation into the defects of the educational system of India set on foot by Lord Curzon, who called a Conference of educational experts at Simla in 1901, raised the question of technical education once more, but the only practical outcome of this was some improvement in the teaching of science at the Universities and the institution of a number of technical scholarships by the Government of India to enable Indians to proceed to England and America. This system also did not work well for

several reasons such as the selection of unsuitable candidates, the difficulties experienced by Indian scholars in getting real practical knowledge in regard to the technique and organisation of industries and the difficulty of providing suitable employment for them on their return. The rules in connection with these scholarships have been recently revised so as to remove some of these defects. In the meantime, the Indian National Congress and the Industrial Conference year after year had been persistently pressing upon the attention of the Government the great need of providing and extending technical education in India.

In recent years the question of technical and general education has figured prominently in public discussions. It received detailed attention at the hands of the Industrial Commission (1916-18), the Calcutta University (Sadler) Commission (1917-1919) and the Committee appointed by the Government of Bombay in 1921. The Industrial Commission made a number of recommendations for (1) the provision of a suitable system of primary education with an industrial bias by local Governments and authorities for the artisan and labouring population including subsidisation of such of the employers of labour as might undertake to supply educational facilities for the benefit of their employees; (2) provision of industrial or craft schools under the control of the Department of Industries for cottage industries and (3) provision for the training of men for organised industries. These are divided into the manipulative industries such as mechanical engineering and non-manipulative or operative industries such as the manufacture of chemicals. The training for the foremen was to be given in the works themselves to which theoretical classes were to be attached, though in some cases like the textile trade in technical schools with workshops attached to them. For the operative industries technological schools were to be started with attainment of practical experience in the factory. In addition to the existing provincial institutions the Commission recommended the establishment of two Imperial colleges, one for the highest grade teaching of engineering and the other for metallurgy and mineral technology.*

* Ind. Comm. Report, Ch. X.

Under the Reforms, education has become a provincial transferred subject. But owing to financial stringency no solid results have been so far achieved in it. Even primary education is making very slow progress in spite of the enabling and compulsory Primary Education Acts that have been passed in several provinces and the raising of the age of employment of children in factories by the Factory Act of 1922. Recognising the necessity of a wider extension of technical education and industrial training, the Government of Bombay appointed a Committee on Technical and Industrial Education in February 1921. The Committee produced two Reports, one by the European Majority and the other by the Indian Minority (the President, Sir Visvesvaraya, supporting the Minority), the main points of difference between the two sections being in regard to types of institutions, number of pupils to be trained and estimates of cost, organisation and agencies for carrying out the scheme and a few minor points. The Majority held the view " that the best means of giving practical training to young men is by establishing apprentice schools attached to large workshops and factories," and put the estimate of the number to be trained in these schools at 600. The Minority object that although such part-time schools attached to the small number of factories and workshops existing at present would be useful to a limited extent, the provision for such a small number would be thoroughly inadequate. They therefore propose " an extension and improvement of the existing system, by the institution of full-time Day Industrial Schools with workshops and laboratories attached " making provision for about 31,000 pupils.

It has not been found possible, however, to take action even on the limited scale contemplated by the Majority Report, though the weaving schools maintained by the Department of Industries continue to help the handloom industry. Thus the present position in regard to general, technical and commercial educa-

\$The Majority also made recommendations for the education of factory children or half-timers in the three 'Rs,' with a practical industrial bias. While the employer's initiative in this respect should be encouraged by Government, the duty of imparting such education should rest with the Government who should, if practicable, make such education compulsory and free.

tion and the actual provision that has been made by Government or private effort can scarcely be called adequate considering the huge size and large requirements of the country.*

\$ 19. Stores Purchase Policy\$:—The various public Departments as well the railways in the country purchase immense quantities of stores of all kinds, many of which were till recently imported from abroad, mostly from England, through the Stores Department of the India Office, London. Government stores imported in 1914-15 were valued at Rs.7 crores, at 16.25 in 1921-1922 and at 9.60 crores in 1926-27. One way of encouraging industries would be to make these purchases as far as possible within the country. Like many another excellent principle this was also recognised long ago without being translated into action. About 50 years ago, Government enunciated the policy of purchasing for state use stores of Indian origin or manufacture rather than stores produced or manufactured abroad. Rules, which were revised from time to time, were also made governing stores purchase, under which preference was to be given to articles wholly or partially manufactured in India, subject to certain conditions as regards quality etc. In cases where the articles available in India are as good as can be had elsewhere and are as cheap as elsewhere, it goes without saying that preference should be given to indigenous goods. There are some who would

* “ There are 153 commercial colleges and schools with 8,157 scholars. The most important among them is the Sydenham College of Commerce in Bombay. Industrial institutions are dotted about in India, some maintained by Government, others by municipalities or local boards and others by private bodies. The most important are the Victoria Jubilee Technical Institute in Bombay, the Indian Institute of Science at Bangalore, the product of generous donations by the Tata family. The tendency in recent years has been to place these institutions under the control of the Departments of Industry. In addition to a number of engineering schools there are engineering colleges at Roorkee, Sibpur, Poona, Madras, Rangoon, Patna, and Benares.....There are schools of art in the larger towns where not only architecture and the fine arts are studied, but also practical crafts like pottery and iron work. There are two forest colleges at Dehra Dun and Coimbatore with 119 scholars in all. A Technical Institute is in existence at Cawnpore and a Mining School at Dhanbad.” *Indian Year Book*, 1928, pp. 389—391.

\$ See Industrial Commission's Report, Ch. XII, *The Indian Year Book*, 1928, pp. 770-772 and *India in 1924-25* 178-189.

go even further than this and would have articles of home manufacture preferred even if they were to cost considerably more. Such a policy would entail an increased burden on the tax-payer and would strictly speaking amount to a grant of protection. And before action is taken under it in favour of a particular industry, opportunity might well be given to the Tariff Board to express an opinion on the matter. In any case, the question would require to be considered in the light of the principles of protection as outlined above. It is not clear whether the rules to which we have referred required a preferential purchase of Indian goods even when their prices were appreciably higher.† However that may be, in actual practice, according to the finding of the Industrial Commission, preference was given to British stores even when they could have been supplied equally well both as regards price and quality by Indian manufacturers, who were handicapped in various other ways in meeting the demands of the Government departments when competing with tenders received by the India Office Stores Department in London. The failure on the part of the Government to avail themselves of the Store Purchase Rules and utilise fully the manufacturing capacity of the country was attempted to be excused if not justified by pointing out that there was no suitable inspecting agency to direct and advise the indenting officer in India, who relieved himself of all trouble and responsibility by sending orders to the India Office Stores Department in London. The explanation provokes

†The latest G. R. on the subject (1928) contains the following instructions:—The departments of the Government of India or the officers expressly authorised by them in this behalf may, when they are satisfied that such measures are justified allow a limited degree of preference, in respect of the price, to articles produced or manufactured in India. Subject to the above, preference in making purchases will be given (a) to articles which are produced in India in the form of raw materials or are manufactured in India from materials produced in India over articles wholly or partially manufactured in India from imported materials or articles not manufactured in India, provided that the quality is sufficiently good for the purpose. (b) to articles wholly or partially manufactured in India from imported materials over articles not manufactured in India, provided that the quality is sufficiently good for the purpose, (c) to articles held in stock in India over those which would need to be specially imported provided that they are of suitable type and requisite quality.

the query why steps were not taken to provide the requisite agency for obtaining expert advice, and cannot be accepted as a sufficient and satisfactory answer to the charge of remissness and anti-national conduct levelled against Government by its critics.† The idea that it is possible to regulate the Stores Purchase policy in such a manner as to stimulate Indian industries was endorsed by the Indian Industrial Commission. Even if the policy of fair field and no favour is adopted without what we may call protective preference being shown to Indian manufactures, the advantage of securing the large custom of Government would in itself act as a healthy and valuable stimulus. Also, as the Industrial Commission have pointed out, if certain suggestions for improving the method of placing orders are accepted, not only would existing industries benefit but also new industries might be started. For example, if instead of allowing unnecessary diversity in orders for the same kind of goods, standard patterns are adopted, it may be profitable to put down special plant in India in view of the large demand for goods of a standard type which would thus result.

With the progress of industrial development it is becoming more and more possible for Government to have their needs supplied by local industries, particularly as arrangements have now been made for removing the difficulty arising from lack of information as to sources and market values of Indian supplies and the absence of an inspecting agency. The Store Purchase Committee appointed in accordance with the Industrial Commission's recommendation supported the latter's suggestion that a central expert agency for the purpose of inspecting Government stores should be established. The Indian Stores Department was instituted accordingly and though it is intended primarily to serve the Government of India, it is open to the Provincial Governments, Municipalities, Port authorities, Company-managed Railways and other public or semi-public bodies and Indian States to avail themselves of its services. The principal officers of the Stores

† Another reasons urged for the policy of Government was that "Manufacturing industries could not be started without a sufficient and continuous market; while orders could not be placed so long as there existed no adequate means of manufacture." *India in 1924-25*, p. 178.

Department as at present constituted are a Chief Controller of Stores, a Director of Inspection, a Director of Purchase and Intelligence and a Deputy Director of Purchase (Textiles). The Department acts in an advisory capacity as a purchase and inspection agency, scrutinises Home indents with a view to preventing orders being placed abroad when purchases of goods of indigenous origin are possible subject to conditions of price and quality; it purchases and inspects certain specified commodities in India, acts as a central bureau of information on all matters connected with the purchase and prices of stores and discharges other important functions so as to encourage Indian industries. Local purchasing branches have been created at Calcutta and Bombay and Inspection Agencies at Madras, Bombay, Karachi, Cawnpore and Delhi. In 1926-27 the value of the purchases effected by the Stores Department was Rs. 3,98,82,000 representing an increase of 45 per cent over the figure for the year before. The Department has adopted and is progressively developing the policy of inviting rupee tenders for delivery in India, for the convenience and encouragement of Indian firms competing with foreign firms. An important part of the work of the Stores Department consists in making continual investigations into the potentialities of indigenous sources of supply resulting in a constant enlargement of the list of approved contractors in India.

CHAPTER II

IMPERIAL PREFERENCE*

§ 1. Imperial Preference a live issue:—The question of Imperial Preference has come much to the fore during the last few years. We propose to discuss it in this chapter and consider particularly how far it is possible for India to participate in the movement for Imperial Preference without unduly hindering her progress along the path of industrial development.

There was a time when an influential section of public opinion in England regarded her overseas possessions as an extravagance for the mother country and injurious to the colonies themselves. The day of the "Little Englanders" is, however, long past, and there is now a universal desire felt in England for drawing the bonds of imperial connection closer together. It is felt that as the manor merged into the town and its surrounding country and as that in its turn merged into the nation, so England must now merge into the bigger unit of the Empire if she is to escape the fate of Holland in the 18th century (Cunningham). As a result of the loss of her American colonies, England's colonial policy underwent a radical change. She realised that she could secure the loyalty of the colonies settled by her own kith and kin only if she granted the fullest political and fiscal liberty to them. The result of complete freedom in fiscal matters was that the self-governing dominions proceeded to levy heavy import duties for protecting their nascent industries against foreign—and particularly British—imports, while England in pursuance of her Free trade policy allowed untaxed admission to the goods of the colonies. The responsibility of protecting the colonies was shouldered almost entirely by Great Britain, and it seemed as if the mother country must be content to typify the normal relations between mother and children by ever offering sacrifices to her colonies without obtain-

* For a detailed treatment of the subject see Fiscal Commission's Report, chap. XIII.

ing any from them. Statesmen like Disraeli feared that the establishment of independent fiscal systems in the colonies with no Imperial Zollverein would infallibly lead to the disruption of the Empire. This prophecy, however, has happily been falsified and the colonies have been showing, in an increasing measure, their appreciation of the invaluable material, moral and political benefits of inclusion within the Empire and have, unasked, granted certain concessions to British goods placing them in a favourable position relatively to the goods of other countries. *Attempts have thus been definitely set on foot for evolving an imperial economic policy and for making as near an approach to Free Trade within the bounds of the Empire as may be consistent with full opportunity to every unit of the Empire to progress along channels marked out by its physical resources and situation.* This provision implies that the policy of protection adopted by most of the countries within the Empire in exclusively national interests is not to be affected by any plan of Imperial Preference. The ideal of immediate Free Trade within the Empire is generally recognised to be "too wild a form of kite-flying to be of any use in practical politics."* Subject to this reservation, however, it is possible that a great deal may be done to promote freer economic intercourse between the constituent states of the Empire so that each may prosper and take a larger part in the life of the Empire as a whole. Foreign countries like Germany, France, and U. S. A. have adopted a high tariff policy, and it has been suggested that the counterpart of this policy has been the exploitation of markets such as those of India and England, which until recently permitted unrestricted entry to foreign commodities. It is claimed that Imperial Preference which postulates the abandonment of Free Trade by the Empire countries is needed not only to fortify imperial sentiment by forging economic links to bind the constituent members closer together but also to act as "a bulwark against the evils of cosmopolitan competition."† In the words of Sir Guy Fleetwood Wilson, "The British Empire may be regarded as consisting not of an aggregate of separate entities with no mutual relations to each

* Robertson: *Trade and Tariffs*, 154.

† Cunningham: *The Free Trade Movement*, p. 168.

other, but of a family of states animated by a common family purpose. Each State in the first instance organises its tariff and its policy to suit its own financial and economic needs, and gives an Imperial sanction to its policy by granting to other parts of the Empire as large a measure of trade advantages over foreign countries as consistent with its own economic development.”*

It is well to recognise clearly certain fundamental points on which there is a general agreement and which are taken for granted in all proposals put forward in favour of Imperial Preference. (1) *The adoption of Imperial Preference should not involve any relaxation or modification of the policy of Protection*, which any of the States may have introduced to foster its industries. In India, before the War, Imperial Preference was favoured by some as the next best alternative to pure Protection, which then seemed unattainable. It meant Free Trade between the United Kingdom and India, the abolition of the hated cotton excise duties and protective tariffs against competitors outside the Empire.† Now, however, India having gained the right of protecting herself even against the United Kingdom, Imperial Preference would mean in practice higher duties on imports from foreign countries than on those from the Empire countries. (2) *The concessions granted to the Empire countries are to be purely voluntary on the part of the country granting them and not dictated either by the mother country or by binding resolutions passed at periodical Imperial Conferences.*¶

§ 2. History of the Movement :—Before discussing the question how far it is possible for India to go in the direction of Imperial Preference, it would be useful to give a brief history of the movement and an idea of the present position with regard to it.

The movement towards Empire trade consolidation may be said to have made a start in 1897, when Canada lowered her duties

* Speech in the Imperial Legislative Council, 17th March, 1913.

† See Sir Roper Lethbridge: *The Indian Offer of Imperial Preference*, p.8

¶ See *Fiscal Commission's Report*, pp. 139-140.

in favour of British goods. In 1898, the preference was fixed at one-fourth of the duty and while it was given to the United Kingdom unconditionally, it was made conditional on favourable treatment to Canada so far as the other colonies were concerned. The Colonial Conference which met in 1902 for the first time adumbrated the policy of Imperial Preference as one of general application to all the parts of the Empire which were invited to fall into line with Canada. Accordingly, preferential duties in favour of Great Britain were introduced by New Zealand and then by Australia, and, love being the price of love, the United Kingdom was expected to reciprocate and grant preferences in return. England, however, was not prepared to depart from her Free Trade policy. She mostly imported raw materials and food-stuffs, and her interests as a great exporter of manufactured articles demanded that she should obtain these in the cheapest market. Especially in the matter of food-stuffs she was not prepared to readjust her customs schedule in a manner that was likely to throw out of cultivation large areas under wheat in Argentina, Russia, Roumania etc., and compel her "to put all her eggs into the one imperial basket." Under the circumstances, the United Kingdom was unable to take any part in the general movement for Imperial Preference. The Self-governing Colonies, however, continued the policy they had begun hoping that the mother-country would find ways of joining in at some future date.

The tariffs of the Colonies have thus come to consist of (a) revenue duties, (b) protective duties, and (c) certain remissions of duty in respect of (a) and (b) in favour of the United Kingdom and in some cases also in favour of India and other Empire countries. There is also a limited free list of commodities taxed only when they come from outside the Empire. As a general rule preferences granted by the Dominions have primarily sought to benefit the United Kingdom, and they have been left to be extended to other parts of the Empire by special negotiations in each case.

Recently, as already mentioned, England has made notable departures in her fiscal policy which have enabled her to grant preferential reduction of duties on Empire goods. From the

Indian point of view the net result of the action taken so far by the different parts of the Empire has been that India is at present enjoying the benefit of preferential rates in some of the Empire countries, viz., Canada, New Zealand and the United Kingdom.

The great War, if it brought forth germs of strength in the British Empire of which it was not sufficiently conscious till then, also revealed at the same time certain vulnerable points in it, and imparted a new urgency to the question of organising the Empire more effectively for peace and war. It was also natural that in an hour of common need and danger the sense of fellowship and common interest was rendered keener amongst the members of the Empire and strengthened the desire of uniting for fiscal and other purposes. The question of Imperial Preference, therefore, has thus been naturally forced to the forefront.

§ 3. Preference and Protection compared:—Preference is in essence a form of protection granted by each of the Empire countries to all or at least some of the rest. And considerations held to justify protective tariffs are almost identical with those urged in favour of a system of preferences. The object may be to assist the country receiving the preference to develop an industry or industries for which it may be well fitted. The development may be expedited if, in addition to securing its own market by the protective duties, the country in question obtains an access to the markets of the sister countries belonging to the Empire on terms more favourable than those allowed in the case of foreign countries. Preferences thus motivated will be temporary and will be made applicable only to those industries that are expected with a little initial help to develop such strength as to be able ultimately to face world competition unaided. Here *as in the case of protective duties the idea is to encourage deserving industries* and not to keep up feeble industries and support them ever afterwards. Again, the industries treated preferentially must be capable after a time of supplying the whole of the demand in the country granting the preference. Otherwise the burden on the consumer will never be lifted. *The only important difference between Protection and Preference is that in the former the consumer's interests are sacri-*

ficed for the direct benefit of some industry in his own country, whereas in the latter case the benefit goes to the producers in the country favoured by the preference.

Like Protection, though in a different way, Preference, besides imposing a burden on the consumer, may also involve a sacrifice of Government revenue even when it takes the form of raising existing duties against foreign goods while continuing to apply the old rate to the goods of the preferred country, for if prices are regulated by the higher rate, the difference between the higher and lower rate goes into the pockets of the favoured producers. *The whole amount of the duty paid by the consumer does not find its way into the government treasury.*

Apart from its uses as an aid to the full development of Empire resources, Imperial Preference is also *advocated as tending to make the Empire self-sufficient.* And, if in the case of at least one of its component states like India, the ideal of self-sufficiency is not impossible, it should be even less difficult of attainment in the case of the Empire as a whole—an Empire on which the sun never sets and which is capable of producing practically every commodity for satisfying all the known human wants. There are, however, bound to be numerous points at which the goal of self-sufficiency will be found to clash with that of economic advantage immediate or ultimate. The value of self-sufficiency in war need not be enlarged upon, and it may be admitted that reliance on foreign countries for essential commodities should be avoided as far as possible. Self-sufficiency, however, should be carried only up to the point where its cost begins to appear prohibitive. Beyond this point the Empire would find “living dangerously” the lesser of the two evils of dependence for the supply of some essential commodities on foreign countries, which may happen to be on the wrong side in the event of a war, on the one hand, and, on the other, an unreasonable and excessive price which must be paid for complete self-sufficiency. It may further be noted that Imperial self-sufficiency is without at least one of the major advantages claimed for national self-sufficiency. If England, for instance, succeeds in producing all the food and other necessary things within her own borders, she may possibly require a smaller navy

than she needs at present for ensuring a regular supply of the needful commodities to her population during war time. Imperial self-sufficiency, on the other hand, would not obviate the necessity of maintaining as costly a navy as at present. England glories in her far-flung Empire, but its far-flung character makes the maintenance of the biggest navy in the world a matter of vital importance—whether for warding off an attack on her possessions or transporting essential goods from one part of the Empire to another.

In short, in assessing the possibilities and determining the extent of Imperial Preference, almost exactly analogous considerations arise to those we had to notice with reference to Protection. *Protection to be really useful needs to be discriminate, a proposition which holds good of Preference also.* The objects of Preference will not be served by extending it to all Empire goods whatsoever indiscriminately. It can be extended only to those industries that satisfy the tests which as we have just seen are very similar to those laid down for Protection, and the extent of the Preference will be governed by considerations of the cost and sacrifice involved.

§ 4. Why India should join the movement:—India cannot afford to stand aloof from a movement in which most of the countries of the Empire are participating. We cannot for the present think of one common fiscal policy of the whole Empire but *a greater co-ordination of the policies pursued by the component units of the Empire is certainly possible and desirable.* Imperial Preference will not only lead to a larger intertwining of economic interests but will teach the Empire to take *effective concerted action in dealing with the outside world.* Imperial Preference will not at once create an Empire customs union with absolute free trade within its boundaries. But, out of the successive concessions granted by each of the constituent states to the rest, a ladder may be framed by which the Empire may climb up to the goal of inter-Imperial free trade, and thus “the largest, richest and most populous free trade area in the world,” may eventually be created.

Since it is generally agreed that India has the best prospects of realising her highest political and economic destiny by rema-

ining a member of the British Commonwealth, she ought to be interested in all projects intended to increase the strength and the solidarity of the Empire. *Her energetic participation in such projects will not merely be a test of loyalty but also of clarity of vision enabling her to see the intangible but none the less important benefits to herself of a strong and well-organised Empire of which she would be a prominent member.* It would, therefore, be her duty as well as her interest to do the best she can in the way of Imperial Preference.

§ 5. The lions in the path:—India is however, less fortunately situated in this respect than the self-governing Dominions. The Dominions having received the gift of self-government from the mother-country are bound to her by ties of gratitude. As between themselves also their relations are most cordial and not marred by any sense of grievance and injustice felt by one Dominion against another. It must be frankly admitted that in India the position is different. She feels that in her attempt to realise her political and economic aspirations, she has been often thwarted and depressed by England, and the anti-Indian legislation enforced by the Colonies against her has naturally embittered her feelings against them. It is indeed arguable that India would gain ultimately by following a generous policy in the matter of giving preferences to Empire countries without immediately seeking an exact *quid pro quo* or making her sympathetic and helpful attitude contingent upon the removal of all kinds of political disabilities from which she may be suffering at the hands of the Colonies. But human nature being what it is, *India's will to do all she is able to for promoting the cause of Imperial Preference is bound to be paralysed to some extent, so long as the more serious political grievances of which she justly complains remain unredressed.* Under the present circumstances, we must expect, while we may regret it for her own sake, that India's attitude towards the question of Imperial Preference should be somewhat unduly querulous and suspicious. The Indian people show a tendency to suspect an ambush in every

proposal in this behalf. * For example, the opposition to the recent proposal for granting a preferential rate to British steel, though it may have been justifiable on other grounds, was undoubtedly largely inspired by a suspicion that England was trying to improve the occasion of giving protection to Indian steel by pushing her own interests in the Indian market. It is thus clear that, however much we may try to keep politics out, they are bound to intrude in discussions about Imperial Preference as affecting India and will have the unfortunate effect of obscuring the real issues, and the steps she may be induced to take in the direction of Imperial Preference will be lacking in spontaneity of impulse and vigour.

The only solution of the difficulty can come with a change of attitude on the part of England and the Colonies. They must show in a practical manner and beyond the possibility of dispute that they are desirous of helping—at least not hindering—India in the task of realising all her legitimate aspirations.

§ 6. The economics of Imperial Preference : India's position:—Hitherto we have urged that India should certainly join the Imperial Preference movement while indicating some of the political difficulties in securing her fullest co-operation. Assuming, however, that she is anxious to do her best we shall now have to consider the question how far it will be within her power to help England and the other members of the Empire by preferences and what direct economic benefits are likely to accrue to herself by preferences granted to her. In this connection it will be necessary to examine briefly the present position as regards India's export and import trade. The following main facts must be borne in mind as being relevant to the question at issue:—

(1) India's imports consist largely of manufactured articles and her exports of raw materials and foodstuffs. (2) About two-thirds of her total imports come from the British Empire, the

* At the Imperial Economic Conference held in 1923, the representatives of India made it clear that India's adhesion to the scheme of Imperial Preference could not be promised on account of her peculiar circumstances which made it difficult for her to adopt Imperial Preference.

United Kingdom contributing by far the largest share* to the imports from the British Empire. (3) Indian exports go preponderantly to foreign countries, only about one-third of the total exports being absorbed by the British Empire. The exports from the United Kingdom amount to about one-fifth of the total exports.† (4) In recent years there has been a tendency towards a gradual *relative* decline of the importance of the British Empire in the trade of India both as regards exports and imports.

The fact that the exports of India consist mostly of raw materials and food-stuffs carries with it the consequence that she does not stand to gain anything much by a system of preferences. For, the demand for raw materials and food-stuffs is keen on the part of foreign manufacturers and there is no necessity of putting forward special efforts for developing a market for them. They are welcome in the foreign markets and mostly admitted free of duty. We must further remember that, if the market for India's exports is confined to the Empire countries, she is likely to obtain less favourable terms than at present, for she now gets the best possible price for them owing to a large number of countries competing for her products.

It is sometimes argued that part of her exports to foreign countries are by way of liquidation of her *indebtedness to England* and that a *direct rather than an indirect method of liquidation* such as would be secured by Imperial Preference is to be preferred as being cheaper. "Why," it is asked, "should consignments not be sent to London rather than to Hamburg or Antwerp and there to enrich a large number of unnecessary middlemen before being sent in manufactured or semi-manufactured form to London?" But as Dr. Marshall points out, "roundabout trade never exists

* The pre-war average percentage of the total imports from the British Empire to the total imports was 69·7 (United Kingdom's share being 62·8), while that in 1926-27 was 54·9 and 47·8 respectively. *Review of the Trade of India*, 1926-27, p. 191.

† The pre-war average percentage of the exports from India to the British Empire was 41·1, the share of the United Kingdom being 25·1, while in 1926-27 it was 38·5 and 21·5 respectively.

without good cause.”* And we may be sure that *Indian exporters would lose by any artificial deflection of the present course of the trade*. They would obtain lower prices for their cotton, jute, hides, skins, seeds, rice etc.

As regards *India's imports* the question to ask is what burdens can she conveniently lay on herself and whether the preference she is able to grant without unduly sacrificing her own interests will be such as to confer substantial benefits on the Empire countries. Here we have to remember that with the help of Protection she hopes before long greatly to diminish her dependence on outside supply and manufacture herself many of the articles which at present form the most important items in her imports. And *since Preference is not to mean any abatement of the amount of protection that may be deemed necessary as a stimulus to home industries and since effective protection implies a rapid reduction of the volume of the competing imports, the Empire countries will suffer along with foreign countries by the shrinkage of the Indian market*. However, so long as substantial quantities of imports continue to come in, the Empire countries will no doubt benefit by the protective duty being raised in the case of foreign imports. The higher duty will mean a greater burden on the consumer already penalised by Protection and, therefore, it cannot be put at too high a level. Even a small difference, however, may be useful and give a decisive turn to the market in favour of the Empire producer. The argument is not essentially different where the duties are imposed for purely revenue purposes. The point to grasp is that *India is a poor country* and the protectionist policy on which she has embarked will require on the part of her population various kinds of sacrifice. The capacity of the country to bear still further burdens on the score of Imperial Preference is strictly limited, and with the best will in the world to further the cause of Imperial solidarity by Preference *the actual concessions*

* “The Continent spins chiefly low counts of yarn and therefore is glad to buy short-stapled Indian Cotton. Who would gain by forcing us (England) to buy short-staple yarn *at relatively low prices* than the Germans can pay, and causing rather more of American cotton to go to Germany ?” (Italics ours) *Memorials of Alfred Marshall*, p. 457.

*she may be able to grant are likely to appear insignificant.** They may nevertheless be welcome as indicating India's desire to do her bit for the Empire and we have already given expression to the view that India should accept the principle of Imperial Preference and try to work it out in her tariff system as far as possible.

When the Government of India were asked in 1903 to examine the question of Imperial Preference from the Indian standpoint, they carefully reviewed every aspect of India's position and came to the conclusion that "from an economic standpoint India had something, but not perhaps very much, to offer to the Empire, that she had very little to gain in return, and that she had a great deal to lose or to risk."† The fear expressed that India had much to lose or risk was largely based on the idea that Preference shown by India to Empire countries would be met by *retaliatory measures against her on the part of foreign countries*, measures which were likely to inflict great injury on her. The Committee of the Imperial Legislative Council, however, which was appointed in 1920 to consider Imperial Preference, came to a different conclusion in this respect and thought that, "in view of the demand for our raw materials, there is no danger to be feared on this score, and that the apprehensions of Lord Curzon's Government in respect of this particular aspect of the question would in present circumstances be unreal."§ As regards one important item of her exports, viz., Jute her monopolistic position places her beyond the danger of retaliation. Her position with regard to many other articles of export though not so strong as in the case of Jute is yet stronger than was imagined in 1902. Any retaliation attempted by foreign countries is likely to imperil their own industries by enhancing the prices of the raw material required by them. Presumably the tariffs already settled by them are such as are best suited for

* The only experiment in India so far in Imperial Preference was the 15 per cent duty devied in 1919 on the export of hides and skins with a rebate of 10 per cent in favour of Empire countries to encourage the tanning industry in the Empire. The experiment however, was short-lived and unsuccessful as will be seen in the next chapter.

† F. C. Report, p. 218.

§ F. C. Report, para 241.

encouraging their industries, and any alteration in them would be prejudicial to their development. No doubt, when strong feelings are aroused, nations sometimes adopt measures even although they may be clearly to their own detriment provided they hit hard the country whose action has evoked resentment. But the tendency at the present time is to regard inter-Imperial trade arrangements such as those contemplated under Imperial Preference as strictly matters of domestic concern, and this is shown by the fact that the preferences already in operation in the British Empire have not been regarded by any of the foreign countries as hostile acts aimed at them. The union of states bound by political ties for fiscal purposes is now looked upon as a perfectly natural arrangement *The danger of retaliation may thus be regarded as negligible.*

§ 7. Safeguards against enforced Preference:—As Imperial Preference implies co-operation of free peoples and not dictation by any outside authority, how shall we ensure, that no concessions are wrung from India by force or against the real wishes of the people? The Majority Report of the Fiscal Commission suggests that all proposals under Imperial Preference must receive the sanction of the Indian Legislature before being put into force. The Minority Report carries caution still further by suggesting that “the power of initiating, granting, varying and withdrawing Imperial Preference, in regard to every article should vest in non-official members of the Legislative Assembly.”

The anti-Indian legislation of the colonies has aroused deep resentment in the minds of the Indian people. And it is perhaps in view of this that the Fiscal Commission's Report is constrained to propose that, while India should offer such preferences as are practicable to the United Kingdom without any conditions attached to them,* she should grant them to the Colonies and

*The relatively more liberal treatment proposed in the case of the United Kingdom is also due to the feeling that “the United Kingdom is the heart of the Empire” and that “the heart will weaken unless the United Kingdom is helped to maintain a prosperous export trade on which its strength depends.” (See Fiscal Commission's Report, p. 143). The recourse to reciprocity agreements suggested in the case of the Colonies may also have been prompted by the idea that no considerable advance in Preference is possible except on

Dominions by special agreements and provided her sacrifices are balanced by the benefits conferred by the other party to the bargain. The Minority Report adopts a more bellicose attitude and advises that "no agreements based even on reciprocity in trade matters should be entered into with any Dominion which has on its statute book any anti-Asiatic legislation applying to the Indian people." The Minority proceed to remark, "Our colleagues point out the fact that Canada and New Zealand have conferred certain preferences on India. To the Indian people their self-respect is of far more importance than any economic advantage which any Dominion may choose to confer by means of preferential treatment. We may confidently state that the people of India would much prefer the withdrawal of such preference as they would not care to be economically indebted to any Dominion which does not treat them as equal members of the British Empire having equal rights of citizenship."*

This is superb but perhaps a trifle unpractical !

a basis of reciprocity. As Prof. Coyajee well puts it "...a system of free concessions...corresponds only to the exchange of ceremonial 'Nazaranas' or complimentary gifts exchanged between exalted personages. No extensive business dealings can be transacted on such a ceremonial basis." J. C. Coyajee : op. cit., p. 170.

* F. C. Report, Minute of Dissent, para 41.

CHAPTER III

INDIAN INDUSTRIES : OLD AND NEW.

§ 1. Scope of the Chapter.—Indian industries may be divided into two classes :—(*a*) Industries carried on in the home of the worker which may be called the Cottage Industries. Here the scale of operations is small, organisation limited and the supplies intended largely for meeting local needs. These we shall discuss at the end of this chapter. (*b*) Organised industries carried on in the workshops or factories which vary in size from simple rural factories carrying out a single operative process to the large textile mills and engineering workshops employing thousands of hands and possessed of a complete organisation, both for manufacture and trade. Organised industries connected with agriculture such as tea, coffee, indigo and sugar industries have been already treated under agriculture.* We shall now first of all attempt a description of the principal organised industries of the new type in India. This will give us some idea of the advance in industrialisation already made and incidentally throw light on the manner in which the new protective system is being applied under the guidance of the Tariff Board.

§ 2. Statistics of Industrial Development :—The following table shows the principal industrial establishments in India in 1921. They include not only the factories but also other establishments which are considered to be of sufficient industrial importance:†—

* See Chapter VII, Vol. 1 above.

†For a more detailed study of the statistics relating to the industries of India the reader is referred to the Statistical Abstract for British India giving the main results of the industrial Census of India taken in 1919 which returned 15,606 as number of establishments (employing more than 20 persons) giving employment to 2,681,125 persons.

Kind of Establishments.	Number	Persons (Thousands)
1. <i>Textiles</i> —		
Cotton Mills	281	346·7
Jute Mills	82	286·9
Woollen Mills	10	5·6
Silk Mills	11	1·9
Cotton Spinning and Weaving ests, not classed as Mills	128	5·7
Woollen Carpet Weaving ests.	21	3·5
2. <i>Minerals</i> .—		
Iron and Brass foundries	101	21·6
Iron and Steel works	1	25·7
Mica works	49	4·4
Petroleum Refineries	11	13·1
3. <i>Transport</i> —		
Dockyards	16	25·2
Ry. workshops and factories	119	149·1
Ship-building and engineering works	9	11·6
4. <i>Food Drink and Tobacco</i> —		
Tobacco factories	34	5·6
Rice Mills	921	61
Sugar factories	71	13·4
5. <i>Chemical dyes &c.</i> —		
Dye-works	26	4·1
Lace Factories	151	9·3
Oil-Mills	225	13·3
6. <i>Paper and Printing</i> —		
Paper Mills	9	6·3
Printing Presses	229	35·8
7. <i>Processes re Wood, Stone and Glass</i> —		
Tile and Brick Factories	467	51·2
Saw-Mills	181	18·2
8. <i>Processes connected with skins and hides</i> —		
Leather works	30	7·1
Tanneries	146	8·6
9. <i>Miscellaneous</i> —		
Cotton-ginning and Cleaning and Press- ing Mills	2043	144·9
Jute Presses	332	37·6
Engineering workshops	222	41·1
Grand Total ...	7514	1559·9

The following statistics are also helpful as affording a measure of the progress of modern industry in India :—

*Indian Factories during 1926 (Subject to the Indian Factories Act.)

Class of concern	Total no. of factories	Aver. daily no. empl.
Government and Local Fund Factories	302	144,519
Textiles:—	408	681,613
Cotton (Spinning, Weaving & other Mills)	273	338,684
Jute Mills	90	332,336
Engineering:—	532	161,892
Railway Workshops	68	76,648
Minerals and Metals	118	55,842
Food, drink and tobacco	2,559	170,585
Chemicals, Dyes etc.	408	46,013
Paper and Printing	285	28,466
Processes relating to wood, stone & glass	335	38,063
Processes connected with skins and hides	36	5,375
Ginning and Presses:—	2,217	178,290
Cotton Ginning and Baling	2,092	145,014
Miscellaneous	51	7,733
Total	7,251	1,518,391

These factories were distributed as follows:—Madras (1,198), Bombay (1,398), Bengal (1,234), United Provinces (313), Punjab (548), Burma (923), Bihar and Orissa (242), C. P. and Berar (677),

* See Annual Statistics of Factories 1916.

Assam (589), N. W. F. Province (17), Baluchistan (5), Ajmere-Merwara (35), Delhi (58), Bangalore and Coorg (14).

The increase in the pace of industrialisation of India since the outbreak of the War may be gauged from the following figures relating to Joint-Stock Companies registered in British India and in Indian States in 1914-15 and 1925-26 respectively.*

Class of Companies	1914-15 No.	Paid- up cap. in lacs Rs.	1925-26 No.	Paid- up cap. in lacs Rs.
Banking and Loan	436	780	885	1,426
Insurance	182	50	67	300
Navigation	24	128	27	273
Railways and Tramways	44	830	48	1,498
Other Transit & Transport	...	...	126	306
Trading & Manufacturing	754	1,132	1,955	8,816
Tea	208	431	401	975
Other Planting Companies	29	41	74	116
Coal Mining	140	609	242	1,175
Gold Mining	8	33	4	8
Other Mining and Quarry- ing Companies	57	576	89	2,987
Cotton Mills	205	1,670	271	3,787
Jute Mills	34	7,61	53	1,639
Mills for Wool, Silk, Hemp etc,	13	122	22	229
Cotton Ginning, Pressing and Baling	...	...	107	236
Jute Presses	139	270	27	172
Flour Mills	30	80	29	135
Estate, Land & Building	32	217	108	712
Sugar (including Jaggery)	22	80	37	201
Other Companies	123	205	354	1,777
Total (British India)	2,480	8,024	4,926	26,779
Total (Indian States)	65	54	385	950
Grand Total ...	2,545	8,078	5,311	27,729

* We have already given statistics of Joint-Stock Companies registered elsewhere than in India but working in India, while dealing with the question of external capital invested in India. See Chapter XIII, Vol. I.

§ 3. *The Cotton Mill Industry :—We shall now proceed to give a short account of some of the large-scale industries in India. The first cotton mill in India was erected at Calcutta in 1818 but the first mill in Bombay, which was destined to be the home of the Cotton Mill industry,† was the result of Parsee enterprise and began working in 1854. Since then the industry has experienced great development and expansion inspite of occasional set-backs due to famine, plague, foreign competition, fluctuations in the foreign exchange and prices of cotton etc.

The early concentration of the industry in the Bombay island has been governed not so much by natural and permanent factors as by other advantages such as the existence of abundance of capital and credit facilities, the presence of cheap and speedy means of transport and the temporary growth of the demand for yarn from China which Bombay was in an exceptionally favourable situation to meet. The year 1877 marks the turning point in the development of the industry from the point of view of its distribution. It saw the beginning of a rapid construction of mills in up-country centres like Nagpore, Ahmedabad Sholapur etc. situated right in the heart of the cotton producing tracts. This later distribution was influenced to a very much larger extent by natural factors such as the vicinity of sources of raw material, labour and large marketing centres, and was made possible by the development of railway communication. The decline of the China trade in yarn from the commencement of the present century also affected adversely Bombay's position of unequalled pre-eminence. The Swadeshi movement, moreover, stimulated the growth of weaving outside the Bombay Presidency. Latterly the developments in Factory Legislation in British India have set up a tendency for the migration of the industry to some of the Indian States where the administration of the Factory Laws is more lax.

* Mr. P. V. Deolalkar has brought together much useful information on the Textile Industries in his Thesis for the Bombay M. A. degree.

† The predominant position of Bombay is shown by the fact that about 74 per cent of the total yarn spun in India is produced in the Bombay Presidency which also is responsible for no less than 87 per cent of the total amount of cloth in the whole of India.

Recently, there has been a tendency on the part of the Indian mills to increase the manufacture of finer counts and a certain amount of long-stapled cotton is imported from U. S. A. and elsewhere for this purpose. But the spinning of finer counts is limited by the expensiveness of foreign cottons as well as that of the new machinery which has to be laid down. An improvement in the quality of the home-grown cotton will help the production of fine counts which is handicapped by reliance on foreign centres for the supply of the necessary raw material.

The cotton industry received a considerable stimulus from the conditions created by the War. The large patronage extended to the mills by the Government in respect of their military requirements in cotton goods in the Eastern theatres of the War, together with the shrinkage in the Lancashire imports into India due to the preoccupation of the Lancashire mills with war-work and the sharp rise in the prices of imported cloth due to shortage of shipping led to a considerable increase in home production, though the difficulty of importing machinery prevented as speedy a development as would otherwise have taken place. As it was, the home-production in piecegoods increased from 1164 million yards in 1913-14 to 1614 million yards in 1917-18. The present production of Indian mills in the whole country is 2258 million yards of woven goods.

The following table brings out the progress made by the Cotton Mills in the whole of India:—

Year	Number of Mills	Number of spindles	Number of Looms	Average No. of hands employed
1877	51	12,44,206	10,385	Not Stated
1900	193	49,45,783	40,124	1,61,189
1914	271	67,78,895	1,04,179	2,60,276
1926	334	87,14,168	1,59,464	3,73,508

The continuous progress of the export trade in yarn till 1904-5 was due to the geographical advantage enjoyed by Bombay

* See *Indian Year Book*, 1928, p. 601.

with respect to the Chinese market. The mills in the Bombay Island supplied more than 90 per cent of the total exports, of which China absorbed 90 per cent. Japan was another important customer till the year 1890. New markets had also been developed in the Straits Settlements and Arabia. After 1905 the trade declined as rapidly as it had developed. The principal factors that led to the decline of our yarn trade were the disturbance in the exchange rates with China consequent upon the closing of the Indian mints to the free coinage of silver, the rise of the spinning industry in China, the shipping difficulties of the Indian merchants caused by the War which gave to Japan her coveted opportunity and lastly the growth of weaving in India itself. It may be noted that Japan did not appear as a rival to India in the Chinese market for yarn till after the outbreak of the War. Since then, however, not only has she succeeded in ousting India from the Chinese market but the imports of Japanese yarn into India itself have increased with alarming rapidity and have seriously affected the prosperity of our spinning industry.

Causes connected with the War led to the memorable boom which started in 1917. It lasted for a period of six years at the end of which the crash came. In the meanwhile, Japan had stolen a march over us not only in the Chinese market but had also begun to pour cheap goods into India which forced down the prices of goods produced in Indian mills. India is now participating in the world depression as it did in the world boom. The boom and the depression in India belong to what is called the Trade Cycle. Other world factors are the altered relations between agrarian and general prices since 1920 and violent fluctuations in the prices of cotton since 1917. The general depression in industry including the textile industry all over the world is the result of the reduced purchasing power of the agrarian classes due to the fall in the world agricultural prices since 1920. Organised manufacturing industries have been better able to resist wage and price reductions than the agricultural industry. Violent fluctuations in prices of cotton in India affected by the American prices and supplies of cotton since 1917 may be held to be another factor which has increased the embarrassments

of the cotton industry in India, While the beginning of the depression was characterised by rising prices of cotton and stationary prices of cloth, during 1925-27 both have fallen in price.* 1923 was probably the worst year for the industry and the depression was so severe that even a succession of three good monsoons combined with the temporary elimination of Japanese competition owing to the earthquake scarcely served to mitigate its severity.

Since the beginning of the present century there has been a remarkable expansion in the weaving industry stimulated by the virtual extinction of the China trade in yarn, and consequently our reliance on foreign cloth has diminished considerably. In 1901 about 63 per cent of the cloth consumed in India was imported from abroad and only 37 per cent produced within the country itself. The percentages for 1925 were 36 per cent and 64 per cent respectively which means that the proportions are practically reversed and the imports have ceased to occupy a preponderant position in the total amount of cloth consumed in the country, though it by no means follows from this that the factor of foreign competition is negligible at the present time.

The position of the trade in piecegoods is in some ways more secure than that of the yarn trade. The weakness of the yarn trade lay in its excessive dependence on one market viz. China, while as regards the export of piecegoods it commands a large number of markets some of which are showing a steadily growing capacity for consuming Indian goods. The diminution in the off-take of a single customer is not, therefore, likely to affect the total volume of the trade to any considerable extent. It must, however, be admitted that Indian industrialists have not hitherto put forth any special efforts to develop foreign markets—an omission which it is all the more important that they should lose no time in making good having regard to the present pitiable state of the industry. The imports of piecegoods have advanced considerably. Here again Japan is a formidable rival as her goods, unlike those of Lancashire, compete directly with Indian manufactures. Japan's ability to undersell the Indian manufacturer is

* See the *Réport of the Textile Tariff Board*, 1927.

due to certain special facilities such as her superior climatic conditions which are conducive to greater efficiency of labour, the larger employment of cheap female labour which social conditions in Japan make possible etc. Further, Japan's cotton purchases are on a large scale and highly organised both in the U. S. A. and India with the Chinese crop in reserve which gives her a considerable advantage over India, though in regard to short-staple cotton, the advantage of course, is on India's side. The mixed Indian and American grey cotton cloth from Japan is more attractive than the Indian stuff. All these can scarcely be called unfair advantages. But this description certainly applies to the consequences of Japan's failure to ratify the Labour Conventions of the Washington Conference in respect of hours of work, prohibition of employment of young persons and of women during night hours. These conditions are inferior in Japan to those in India, and they will remain so at any rate till the Japanese Factory Law of 1926 comes into operation in June 1930, though even then Japan will enjoy certain advantages as regards hours of work. "Double-shift working in Japan gives Japanese industry an advantage of 4 per cent on the actual cost of manufacture both of yarn and cloth. This advantage is considerably increased if a reasonable return on capital is included in the cost of production."*

The difficulties of the cotton industry have been enhanced by the frequent changes in the currency policy since 1893 and the latest change of the ratio from 1s-4d to 1s-6d has undoubtedly hit the industry very hard at a time when practically the nadir of depression had been reached. Regarding the effect of depreciation of Japanese exchange on her competition with India, the Tariff Board held the view that it did stimulate Japanese exports to India while it lasted from December 1923 to December 1925, but that thereafter Japan had ceased to enjoy any special advantage in this respect.

The depression in the cotton mill industry is also to some extent attributed to certain defects of external and internal organisation. Under the first heading may be mentioned the un-

* Report of the Textile Tariff Board.

satisfactory Managing Agency System, and as an instance of the second, we may refer to the absence of any satisfactory system of finance, which has seriously inconvenienced both mills and dealers. The Managing Agency System has come in for a good deal of damaging criticism and a few words about it may be permissible. The Managing Agency is a private partnership of three or four members usually related to each other. The ownership of the Agency is governed by the hereditary principle, so that management often passes into incompetent hands. The managing agents hold a large number of shares in the mill and make themselves responsible for the financing as well as management of the mill, the purchase of supplies and the sale of the goods. Some of the methods of remunerating the Agents are apt to lead them into action which, while it adds to their private gain, is prejudicial to the interests of the mill. For example, where their commission is based on the total volume of production, the interests of the Managing Agents lie in swelling the output as much as possible irrespective of the effect of such a policy on the profits of the mill. The Managing Agents have also been charged with taking secret commissions in the course of the buying and selling transactions which they undertake on behalf of the mill. There can be no doubt that this system needs to be overhauled so as to bring about a greater identity of interests between the mill and the Managing Agents.

The depression has been especially acute in the case of Bombay owing to circumstance already mentioned viz. the virtual loss of the China trade in yarn owing to Japanese competition and the expansion of the Chinese industry (a loss not wholly compensated by an increase in the export of piece-goods), difficulties of freight during and after the War, and the increase in the severity of internal competition from up-country mills which have shown a remarkable expansion during recent years. No doubt part of the blame for this rests on the Bombay mills which have paid insufficient attention to up-country markets in respect of diversification of production, especially in higher counts, more direct contact with the consuming centres and greater alertness on the part of commission agents. But Bombay

also suffers from certain serious disabilities for which she cannot be blamed, viz. her relatively higher cost of labour, fuel, water, power, high local taxation, distance from the mofussil markets and from sources of raw material.

§ 4. The Textile Tariff Board.— In June 1926, the Government of India appointed a special Tariff Board to inquire into the causes of the depression in the cotton industry in Bombay and to make recommendations regarding the advisability of the grant of protection to the industry which had been demanded by the Bombay Millowner's Association. The Board's findings regarding the causes of the depression have been already indicated above. Some of the remedies suggested by the Board are a better organised purchase of raw material, e. g., under a single hedge contract system; adoption of various devices to obtain a greater output from labour, such as the piece-work system, greater care in recruitment of labour, better housing and education for the labourer etc. Other suggestions are more efficient organisation and more of combined action for furthering common interests on the part of millowners, greater diversification of production and more specialisation in products of higher counts so as to take full advantage of the damp climate and the favourable situation of Bombay in respect of the imports of long-stapled American and African cotton. The Board also suggest that the development of new lines of production e. g. the establishment of the cotton printing industry, more attention to the development of promising markets such as Persia, Mesopotamia and the maintenance of a closer touch with consuming centres in India as well as abroad, will considerably mitigate the existing depression in the Bombay Industry.

As regards protection, while the Board were opposed to a differential duty against Japan alone as being undesirable, they held that so long as labour conditions in Japan continued to be inferior, a moderate measure of protection both for yarn and cloth in addition to the protection afforded by the present import duty of 5 per cent on yarn and 11 per cent on cloth would be justified. They recommended different methods for the protection of cloth and yarn, as they thought that an additional duty on yarn would adversely affect the important hand-loom industry, (which

in 1925 supplied about 26 per cent of the total consumption of cloth in India,) as also those mills that have weaving sheds only. They proposed, therefore, that while the cotton manufactures other than yarn should be protected by an addition of 4 per cent to the present duty on corresponding foreign imports for a period of three years, a bounty should be granted for four years on the spinning of higher counts of yarn, subject to certain conditions in respect of the counts spun. The additional advantage claimed for a bounty over an import duty is that it gives direct and measurable help, offers a greater stimulus than an import duty and does not altogether remove the healthy influence of foreign competition. The Board also recommended the restoration of the concession of free entry enjoyed by cotton mill machinery and mill stores prior to 1921. An item of state-aid proposed by the Board is that Government should give assistance to a combined bleaching, dyeing and printing plant, if a satisfactory scheme is put forward by the Bombay Millowners' Association, either in the form of a loan free of interest for a period of ten years, or Government guarantee of interest or subscription of as much capital as is subscribed by the public. The Tariff Board also recommend the appointment of two Trade Commissioners, one at Basra and the other at Mombassa and a rapid survey of the potentialities of other markets by a small Trade Mission including a representative of the Millowners' Association. A further suggestion is that Government should meet a portion of the expenditure incurred by the Millowners' Association for maintaining its own representatives in foreign countries.* The Board suggest that the cost of some of the above proposals should be met from the proceeds of the additional 4 per cent import duty on cotton manufactures other than yarn. The import duty thus claims a double

* The Board were hostile to certain proposed methods of assisting the cotton industry, such as the levy of an export duty on cotton, grant of bounties on export of yarn and piecegoods and abolition of the Company Super-tax. However, they recommended an inquiry into the proposal of the Millowners' Association that provision should be made for granting subsidised shipping freights as in Japan to promote the export trade.

advantage; it is most suitable for meeting the cost of the Board's proposals and as giving a definite stimulus to the industry, and it exactly offsets the actual advantage (without, however, including a reasonable return on capital) enjoyed by Japan as a result of the double-shift working.

§ 5. Mr. Noyce's Minute of Dissent:—Mr. Noyce, the President, while agreeing with his colleagues regarding the desirability of stimulating spinning of yarn of higher counts in Bombay and of giving protection to the industry against unfair Japanese competition, does not approve of the scheme of bounties proposed by the Majority. He holds that in addition to certain insuperable administrative difficulties involved in working the scheme, there are several fundamental objections. A long established industry does not need artificial stimulus for a development which is in its own interests. It is likely to have some undesirable effects as is implicitly admitted by the proposal to limit the bounty to 15 per cent of the spindles in a mill. It would do little good to mills having spinning departments only, as the price of Japanese yarn would remain unaffected which competes with at least 87 per cent of the production of yarn in Indian mills. It is not likely to be of special value to Bombay mills, as it will not protect them from the competition of the up-country mills which are in a position to avail themselves of the bounty. Moreover, Mr. Noyce thinks that the difficulties in regard to suitable raw material have been underestimated and that the effect of the subsidy would be unequal as between the various cotton centres and even in the different mills in the same centre.

He is also opposed to an all-round increase in the import duty by 4 per cent as he does not approve of its major justification, viz., the provision of funds for a bounty on yarn, and holds that the abolition of the cotton excise has made it unnecessary to offer any help for adjustment between high wages and low prices. Nor does such a duty offer any help against the competition of up-country mills which do not require protection so badly as the Bombay mills. He concludes that " the maximum duty which can be justified is one which will offset the actual advantage per pound of yarn or per pound of cloth manufactured, derived from double-shift working

in Japan." As there is no logical ground for distinction between yarn and cloth, he recommends the imposition of a differential duty of 4 per cent on all cotton manufactures imported from Japan at the earliest possible date from which such duty can be imposed with reference to the terms of the Anglo-Japanese Convention of 1905. The duty should continue until the end of the year 1929-30. Mr. Noyce concludes, that on its merits, apart from the wider question of Imperial Preference, the imposition of a duty on the imports of cotton manufactures from non-Empire countries would be preferable to a differential duty against Japan alone.

§ 6. Government action on the Report:—* Reviewing the Report of the Board in a Resolution (dated June 7, 1927) the Government of India endorsed the view of Mr. Noyce that the proposed bounty scheme was impracticable and, therefore, its rejection removed the chief cause for a general increase in the import duty on piecegoods. They held that the advantage to Japan, if a reasonable return on capital were included in the cost of production, was 10 per cent and was thus more than covered by the existing 11 per cent revenue duty on cloth. Therefore, no additional duty on this account was justified. Though the existing 5 per cent duty on imported yarn did not fully cover the advantage of Japan, an additional duty was undesirable in view of its prejudicial effect on the handloom industry. Government, however, approved of the Board's recommendations regarding the removal of the import duties on machinery and mill-stores, but as differentiation between one industry and another was undesirable proposed to remove the import duty on all machinery and on certain mill stores.

This disappointing decision raised a storm of protest and indignation in Bombay and other centres, and Government were roundly charged with callous indifference to the welfare of the one great truly national industry. They were taken to task for not accepting the recommendations of their own Board—either of the Majority or of the Minority. A conference of the representatives of the industry met in Bombay and a

* See Indian Year Book, 1928, pp. 724-25.

deputation of the Millowners waited on the Viceroy. Government were thus prevailed upon to reconsider their decision and they announced on August 16, 1927, that "they had come to the conclusion that the cotton spinning industry could fairly claim additional protection and that they had decided to bring before the Legislature a Bill providing that up to 31st March 1930, the duty on cotton yarn, irrespective of the country of origin, should be one and half annas per pound or 5 per cent ad valorem, whichever was higher. This meant that a specific duty was to be imposed on imported yarn, unless its value exceeded Rs. 1-14-0 per pound, in which case it would continue to be 5 per cent ad valorem." It was further decided to reduce the existing import duty on artificial silk from 15 to $7\frac{1}{2}$ per cent so as to give some relief to the handloom industry in view of the burden imposed on it by the revised import duty on yarn. It may be noted in this connection that the handlooms and cotton mills in India are using increasing quantities of such artificial silk. Lastly, the list of mill-stores to be exempted from duty was to be extended. Accordingly, two Acts amending the Indian Tariff Act were passed in the September session of the Indian Legislature (1927) embodying these decisions regarding (i) imported yarn and (ii) machinery etc. respectively. The Government of India have also appointed a Commercial Mission as suggested by the Board. All this, however, has not satisfied either the Mill industry or public opinion in India. The depression in the industry still continues and the general feeling is that more substantial help is needed.

§ 7. The Jute Industry:—The first Jute spinning mill was started at Rishra near Serampore in Bengal in 1855, and the first powerloom was introduced in 1859. The progress of the industry was slow during the first thirty years or so and there was scarcely any export trade in jute manufactures. There were, however, not wanting periods of great prosperity enjoyed by the industry falling within this initial stage of comparatively slow development. From 1868 to 1873, for instance, "The mills simply coined money," and paid dividends ranging from 15 to 25 per cent. This led to the establishment of a large number of new mills and to overproduction. Consequently, profits declined rapidly. The industry passed through a crisis and a number of

mills had to be closed down. The Jute industry, however, had reached large dimensions and in 1881 there were as many as 5,000 powerlooms at work in Bengal. Since 1885 has been discernible a tendency towards a larger output of hessian cloth than gunny bags. Between 1877 and 1915, while sacking looms increased from 2950 to 17,750, the hessian looms increased from 910 to 22,603, i.e. there was a growth of 2,400 per cent in hessian looms as against 430 per cent in sacking looms.* The War led to a considerable expansion and prosperity of the Jute industry, which was called upon to meet the demands in the various theatres of the War for sand bags for the trenches and Jute canvas cloth for war purposes such as tent cloth, tarpaulins, waggon covers etc. This new development was stimulated by the necessity of substituting jute for the Russian flax whose supply was largely cut off by the overrunning of Russia by Germany in 1915-16.¶

Barring minor vicissitudes the story of the Jute industry has been one of steady and continuous progress. In 1891 there were 8,000 power looms at work in Bengal : in 1901, 16,000 ; in 1911, 33,000; in 1921 43,000 and in 1925-26, 50,503‡ The following statistics further bring out the remarkable progress made by the industry, especially during and since the War :—

	Number of mills at work	Authorised capital in lakhs of Rs.	No. in thousands.		
			Persons employ- ed	Looms	Spindles
Average					
1879-80 to 1883-84	21	270.7	38.8	5.5	88
1899-1900 to 1903-04	36	680,	114.2	16.2	334.6
1909-10 to 1913-14	60	1,209	208.4	33.5	691.8
1914-15 to 1918-19	73	1,403.6	259.3	39.7	821.2
1925-1926	90	2,134.7	331.3	50.5	1,063.7

* Deolalkar : *Textile Industries in India*.

¶ Industrial Handbook, Indian Munitions Board pp. 365-366.

‡ See Industrial Comm. Report, p. 10 and The Statistical Abstract for 1925-26.

For many years Great Britain was the only country which manufactured jute goods, Dundee being the principal centre of manufacture. Calcutta has now taken a large part of the trade held by Dundee in the past. The Indian mills consumption of jute is about five times as much as that of Dundee. The value (52.83 crores of Rs.) of jute manufactures exported by sea in 1926-27 was over 42 times as great as the average value (1.2 crores of Rs.) of the export in the period 1879-80 to 1883-84.

The demand for jute goods depends on the volume of agricultural production throughout the world, jute manufactures being required for moving agricultural produce from one place to another in the course of internal as well as international commerce. A favourable agricultural season in India leads to a shrinkage of exports of jute manufactures as the demand for packing material increases within the country itself for moving the large volume of crops. The Jute and Cotton manufactures are outstanding examples of the progress of modern large-scale industries in India, each of which gives employment to about 350,000 persons, jute being an Indian monopoly. The position of the Jute industry in international trade is much stronger than that of the Cotton industry. As already pointed out, one remarkable contrast between these two most important organised industries of India is that, while the Cotton mill industry is almost entirely in Indian hands and financed by capital raised in India, the Jute industry owes its origin and development to European—mostly Scottish—enterprise and capital. Another point of difference is that while the Cotton industry is decentralised, the Jute industry is highly centralised, there being as many as ninety jute mills within a radius of forty miles.

As *Dr. Pillai observes, “in point of efficient organisation, the jute industry is perhaps second to none in India.” The Indian Jute Mills’ Association was formed in 1886, among other things, to facilitate the adoption of concerted action, for example introduction of short-time working in the mills to avoid over-production etc. In 1921-22 the post-war slump led the Association

Indian Year Book, 1918, p. 701.

† Dr. Pillai : *Economic Conditions in India*, p. 175.

to invite an American business expert to advise it on the possibility of forming a jute trust with a view to exercising some control over the production and price of jute. The termination of the slump, however, led to the abandonment of the project for the time being. It may be noted in passing that the Bombay Cotton Millowners' Association also is becoming alive to the importance of concerted action as shown by the proposed scheme of standardisation of wages which was put forward during the strike in Bombay just ended. The Calcutta Jute Dealers' Association looks after the common interests of its members as dealers in jute for local consumption.*

§ 8. Iron and Steel Industry:—The Iron and Steel industry has a better claim than almost any other to be called a basic or 'key' industry and its national importance cannot be exaggerated. A striking contrast between the Industrial Revolution of India and of England is that, while the Revolution began in India with the application of steam to the textiles, it began in England with the development of the essential iron and steel industries. The new industrial system in England had a solid foundation in the firm establishment of the iron and steel industry and the ancillary mechanical engineering industries. But such a development has not marked the course of the Revolution in India. Until recently Indian industries have relied almost exclusively upon imported machinery and machine tools, and hardware goods in general. However, both Government and the public have at last waked up to the extreme importance on national grounds of the iron and steel industry, and certain important steps to be alluded to presently have been taken to ensure its rapid progress.

Pioneer attempts to introduce modern methods for the manufacture of pig iron and steel were made as early as 1830 in the South Arcot district. They were all destined to failure until the Barakar Iron Works, which were acquired in 1889 by the Bengal Steel and Iron Company, were started in 1874 in Bengal on the Jherria coal fields. The Bengal Steel and Iron Company

* Indian Year Book, 1928, p. 704.

began to show a profit balance only from 1899. The annual production at the beginning of the present century was about 35,000 tons. An attempt to make steel resulted in heavy loss owing to the low price of imported steel, small orders for numerous sections, inferior quality of pig iron then produced for steel-making and dependence on imported supplies of fire-bricks and ferro-manganese.* A new era in the history of the Bengal Company, however, was opened in 1910 with the beginning of the exploitation of a new source of iron ore in the Singhbhum and Manbhum districts.

The next important stage in the history of the industry was ushered by the formation of the Tata Company. The Company was established at Sakchi in the Singhbhum district by the late Mr. J. N. Tata in 1907, and the construction of the work began in 1908. Pig iron was first produced in December in 1911, and steel—for the first time in India in modern times—in 1913; and by 1916 under the stimulus of the War demand, the old plant was in full production. Thus after a somewhat anxious period, which was to be expected in a pioneer enterprise of this character, especially in the face of unfettered foreign competition, the works were placed on a sound footing and proved of invaluable assistance in prosecuting the War by providing large quantities of rails and sleepers for military railways in Mesopotamia, Palestine, East Africa and Salonika. In 1917 a large scheme of extension was mooted and completed in 1924, the delay being the result of difficulties of the War and the post-War periods, such as that in connection with the import of the necessary machinery. The old plant turned out finished steel products, such as rails, heavy structurals (beams, angles, channels), bars, light structurals, light rails and fish plates. The additional products which the new plant, already set into operation since 1926, is meant to turn out, are plates, sheets (black and galvanised), sheet bars and sheet sleepers.† The success of the Tata enterprise has called into existence some new companies, such as the Indian Iron and Steel Company formed in 1908 by Messrs Burn and Co. of Calcutta at Hirapur near Asansol, the United Steel Corpora-

* Industrial Handbook of the Munitions Board, pp. 138-139.

† Report of the Tariff Board on the Steel Industry, 1924, paras 14-15.

tion of Asia (1921) started by Messrs Bird and Co. of Calcutta at Manoharpur, the Eastern Iron Company and the Mysore State Iron Works at Bhadravati (1923). It may be noted that at the last named works blast furnaces are blown by charcoal.

The expansion of the industry is reflected in the figures of production and imports. The production of pig iron advanced from 35,000 tons at the beginning of the century to 162,282 tons in 1914; 232,368 tons in 1919 and 957,000 tons in 1926-27. In the latter year 309,000 tons were exported, Japan being the principal customer for India's pig iron. The quality of the pig iron turned out is fully equal to that of the Continental product; indeed the imports of pig iron are now almost negligible being 1,627 tons valued at $2\frac{3}{5}$ lakhs of rupees in 1926-27.* It is calculated that when the several Companies mentioned above are in full working order they will have a total output of 1,500,000 tons of pig iron and 1,000,000 tons of steel annually.¶ The production of steel advanced from 370,000 tons in 1924-25 to 530,000 tons in 1926-27.

While India is still dependent to a very large extent upon foreign iron and steel, her own increasing production is shown by her steadily decreasing imports. In 1913-14 she imported 1,018,000 tons of steel and iron manufactures, 427,000 tons in 1919-20 and 845,000 tons in 1926-27. The fall was specially noticeable during the War period when the Tata Company increased its output and supplied the Government with war materials. The post-war increase in the imports furnished an added plea for protection being granted to the industry.

Before turning to the question of protection let us refer to some striking developments in connection with the establishment of subsidiary industries including those utilizing by-products in the neighbourhood of Sakchi (renamed Jamshedpur at the end of the War). The following are some of the various manufactures which it is intended to produce under the Extension

* Review of Trade, 1926-27.

¶ Pillai: op. cit. p. 223.

Scheme:—steel tubes, tinplate, enamel ware, wire, nails, railway wagons, tea and jute mill machinery, agricultural tools, galvanised products, iron and steel castings, heavy chemicals, sulphuric acid, nitric acid, fertilisers, lime, ammonium sulphate etc. Various manufacturing companies have already been established for this purpose. Jamshedpur and the surrounding territory are thus developing into a veritable beehive of modern industries.

§ 9. Grant of Protection to the Steel and Iron Industry:—The policy of discriminate protection adopted by the Assembly early in 1923 was brought into operation for the first time in India in the case of the Steel and Iron Industry. The first task with which the Tariff Board was entrusted was that of investigating the claim put forward by the Tata Steel and Iron Company for protection to the steel industry. The Company proposed that the existing 10 per cent *ad valorem* import duty should be raised to $33\frac{1}{3}$ per cent in order to give the industry adequate protection against the dumping of foreign steel and iron, which was stimulated by the depression in the world trade, depreciated continental exchanges and the long start which the well-established foreign industry had obtained over the infant industry in India. They further drew attention to the opinion of the Fiscal Commission that the prosperity of such an important basic industry was essential from the point of view of national safety and development, and recalled the great services rendered by them to the Government during the late War.

The Board after a careful inquiry came to the conclusion that the case for protection was not ill-founded, and that development had been recently hindered by severe competition from abroad coinciding with a large scheme of expansion set on foot by the Tata Company. The Board held that the industry satisfied all the conditions laid down by the Fiscal Commission. India possesses great natural advantages for the manufacture of steel owing to the richness and abundance of iron ore deposits in the Sinhbhum and Orissa Iron belt and the comparatively short distance which separates them from the coal-fields. The

quantities of coking coal available are sufficient for the requirements of the country. Similarly, the supplies of limestone and dolomite are ample and good enough for most purposes. Most of the other raw materials required, such as manganese* and materials for refractory bricks exist in India in sufficient quantities. The industry also possesses the advantage of a large and expanding home market. In respect of labour, however, "India suffers under a disadvantage inevitable in any country mainly agricultural, and where industrial experience and training has still to be acquired," rendering it necessary to import at present skilled supervisors from America and Europe. This is, however, a temporary handicap which would eventually disappear.† The Board held that, unless protection was given, there was no hope of the industry developing for many years to come, and there was a serious danger that it might cease altogether. It was also thought that probably the cost of steel production would fall substantially in the next three or four years and that the industry would be able to do without protection at no very remote date. The Board agreed that it was also an essential industry for military purposes, and was, therefore, specially entitled to protection.¶

The Steel Protection Bill incorporating the recommendations of the Board was considered and passed by a special session of the Indian Legislature (May-June, 1924). The duties on certain articles manufactured from steel were increased, and bounties were granted on heavy steel rails, fish plates and railway wagons

* See Chapter II, Vol. I above.

† In this connection it is worth while quoting the testimony of Sir Thomas Holland who said, "Any one who has visited the Tata Steel and Iron Works will come away thoroughly convinced with the conclusion that with Indian labour you can tackle any industry for which the country is suitable. I have seen labourers at Sakchi who only a few years ago were in the jungles of Santals without any education. They are handling now red-hot steel bars, turning out rails, wheels, angles of iron as efficiently as you can get it done by any English labourer. You cannot have a better test of the quality of labour, and you cannot be prepared for more satisfactory results."

¶ Report of the Tariff Board (Steel), p. 82,

manufactured in India. For instance, the duties on steel bars were fixed at Rs. 40 per ton, and on sheets at Rs. 30 per ton. The bounties, which were fixed at diminishing rates per ton on steel rails and fish plates produced in India were fixed at Rs. 32, Rs. 26 and Rs. 20 per ton respectively in each of the three years for which the arrangement was to be operative. At the end of the period, the bounties and duties alike were to be subject to revision. During this period the steel industry was expected to attain its full production, and it was also anticipated that world conditions would be stable after the lapse of three years and the data for the subsequent inquiry would be more satisfactory.* The burden on the consumer was expected to be temporary and widely diffused and not too heavy considering the advantages to be gained.

Subsidiary measures of protection had to be taken to safeguard the interests of such of the industries as make use of steel as their raw material. An increase in its price resulting from the grant of protection, was likely to be detrimental to many branches of the engineering industry at a time when it was holding its own with difficulty in the face of foreign competition. The Tariff Board made certain recommendations to meet this aspect of protection to steel which were accepted by the Government and the Assembly. The Engineering industry was protected by higher duties on imported fabricated steel. A 25 per cent *ad valorem* duty was levied on fabricated steel with certain exceptions. The Wagon industry was protected by bounties for five years on an increasing number of wagons but at a decreasing rate. The Tinplate industry was protected by a specific import duty of Rs. 60 a ton (i. e., 15 per cent *ad valorem* instead of 10 per cent). The manufacture of steel wire and wire nails was protected by specific duties of Rs. 60 a ton on certain classes of wire and nails. The proposal of the Board that the manufacture of agricultural implements in India should be protected by raising the 15 per cent *ad valorem* duty to 25 per cent on certain classes of implements was negatived by the Assembly as likely unduly to injure the interests of the agriculturists. The Board did not

* India in 1924-25, pp. 169-170.

for various reasons accept the claims put forward by the Locomotive, Steel Castings and Enamelled Ware industries. For instance, in the case of the Locomotive industry, the home market was restricted, though in the opinion of the Board the industry deserved Government assistance.

The protection granted to the Steel industry was, however, soon afterwards largely nullified by the fall in the price of Continental steel and the maintenance of the exchange in the neighbourhood of 1s 6d. The Board, to whom the question was referred, reported that the case for further protection was well-founded and suggested an enhancement of the duties. The Government of India, however, preferred a bounty which, while of immediate benefit to the industry, would not raise the price of steel goods in the country. The Government proposals were accepted by the Assembly in 1925. Accordingly, provision was made for the grant of a bounty at the rate of Rs. 20 per ton on 70 per cent of the weight of steel ingots suitable for rolling into articles already protected by duties in the previous May and produced in India from Indian pig iron between 1st October, 1924 and September 30th, 1925. The funds for the bounty were to be supplied from the proceeds of the increased import duties imposed in May.

§ 10. Statutory Inquiry into the Steel Industry:—As provided for by the Steel Protection Act, 1924, which was due to expire on 31st March 1927, the Tariff Board was directed in 1926 to make an inquiry as to the necessity for further continuance of protection and the degree of protection required. The Board after a careful examination of the whole question recommended the continuance of protection on certain lines for a further period of seven years. The industry was to receive protection in the form of increased duties on imports and not by bounties on production, since the latter would be too costly to maintain over a period of seven years, at the end of which a fresh inquiry was to be made in order to ascertain what kind and amount of protection might still be necessary. Accordingly, a Bill was introduced in the Delhi Session (1927) and came into force on 1st April 1927. It "provided for an imposition of *differential* rates on certain iron and steel articles with a basic duty on articles of British manu-

facture and an additional duty on those of non-British origin.”* There was a heated debate in the Assembly on the proposal to differentiate between standard and non-standard steel, that is, practically between British and Continental steel. Government agreeing with the Board held that this was necessary in order to secure a fair distribution of the burden on the different classes of the consumers and to ensure stability to the scheme of protection. The Opposition suspected that the Bill contained the principle of preference to British steel to which they were opposed. The alternative suggested in the Select Committee, (viz., a uniform rate of duty based on the weighted average price of imported steel) was thrown out by the majority. Government were opposed to it on the ground that it would offer inadequate protection and would also enhance to an unnecessary extent the price of standard steel, as well as of fabricated steel in India. This would hinder development work throughout India in respect of bridges, public works and manufacture of machinery. The British and Standard Steel happened to be synonymous, but by levying differential duties on British and Continental steel, the administrative difficulties in testing every consignment of steel imported into India for the purpose of levying differential duties on standard and non-standard steel were obviated. The Assembly passed the Bill as submitted by the Majority of the Select Committee which, however, succeeded in introducing two safeguards providing that the Governor-General-in-Council may increase, but not reduce the duty chargeable on articles of British manufactures so as to ensure effective protection and that he may order an enquiry into the Steel Industry earlier than 1934 if he thought it desirable.†

In 1928, March, Government introduced a Bill to give effect to their decisions on the Tariff Board's Report regarding the protection to Steel industry (wagons and underframes). It was argued that the policy of protection had in this case succeeded and that the industry would, with some further protection, be able to stand on its own legs. The Bill has been referred to a Select Committee. It does not, however, provide for any protec-

* See India in 1926-27, pp. 70-72.

† *Ibid.*

tion to the wire nail industry on the ground that the raw material for this industry was not being produced in India and the only firm which had been manufacturing nails had closed down. The steel castings were not given protection in spite of the Board's recommendation, because it had been ascertained that the position of the industry was such that it could not develop to any great extent by means of a bounty. This decision of the Government was adversely criticised and it was argued that the case of the one firm engaged in this industry should have been more carefully considered. The Government were taken to task for not respecting the findings of their own Board in this respect.

On the whole, we may approve of the general policy followed in regard to the Steel and Iron industry during 1924-27. There is no doubt that without the timely intervention of the State the industry could not have survived the shock of post-war competition. Perhaps the protection offered between 1924-27 was not quite adequate and the Tata Steel Company was barely able to pay its way. In spite of certain unfavourable circumstances, however, the industry made appreciable progress as "evidenced by increase of output, improvement in the efficiency of labour, reduction in the number of foreign hands, and considerable reduction in works costs" and also by "considerable improvement in the conditions of labour, especially in respect of wages, housing and various amenities of life."¹ On the whole, therefore, the decision to continue the protection for another seven years would seem to be abundantly justified, and there are grounds for hoping that at the end of this period, the steel industry will find its legs and dispense with the crutches of protection.

§ 11. Tanning and Leather Industries:—India possesses a large supply of hides and skins. The cow-hides ('the East India kips' as they are called), goat-skins, buffalo-hides and sheep skins etc. may be regarded as the by-products of her agricul-

¹ See Article on the Protection of the Steel Industry, 1924-27, by Mr. H. L. Dey, Indian Journal of Economics, July, 1928.

tural industry. Previous to the War, India sent out large exports of raw hides, especially to Germany and Austria, which were valued at Rs 7.17 crores in 1913. In the same year, raw skins valued at Rs. 3.40 crores were exported, mainly to U. S. A. There was a large demand in foreign countries and high prices were offered. The War brought about important changes in the Indian Tanning industry and in the export trade in hides and skins, partly because of the cutting off of the enemy markets and partly owing to the control exercised by Government.

Before reviewing the war-time and post-war developments a short history of the industry may be given. There has existed since long a considerable indigenous tanning industry in the country under which locally available tanning materials are used for curing and tanning hides mainly to meet the local demand for inferior kinds of leather. But the most striking changes have taken place in the European methods of tanning which were first introduced by the military authorities to manufacture superior leather suitable for harness and other military requirements, and tanneries usually followed the establishment of arsenals. At Cawnpore, a further step in production was taken in 1860 when the Government Harness and Saddlery Factory was set up. Shortly afterwards, Messrs Allen and Cooper established the Army Boot and Equipment Factory and received at the outset considerable financial assistance from Government. "A marked degree of success has attended the efforts to develop the leather trade in Cawnpore, and, up till the time of the outbreak of the war, the factories which have come into existence, though largely dependent on the army for orders, were by no means appanages to the military department."* The Western India Army and Equipment Factory was started at Sion in Bombay by Admjee Peerbhoy. A few more factories were established at various centres where the production of finished goods was attempted.\$ Although considerable use of machinery is made in European tanneries and leather-working factories, it was until recently conspicuous by its absence in the Indian tanneries except in the Cawnpore and

* Appendices to the Ind. Commission's Report, p 57.

\$ See Pillai op. cit. p 178

Sion factories and the Madras Tannery, which produced the whole of the half-tanned leather and skins that loom largely in the export trade of the country. Before the War, the bulk of the export trade in tanned hides and skins was confined to the South of India where the bark of *cassia auriculata*, known in Madras as *avaram* and in Bombay as *tarwad*, is obtainable, Madras having by far the larger number of tanneries.

§ 12. Effects of the War on the Tanning and Leather Industry:—The tanning and the leather industry underwent a remarkable transformation during the War. The Indian Munitions Board directed its activities towards increasing the outturn and regulating the production of those kinds of leather which possess a special value as war material. The most important development was connected with the great increase in the production of the rough-tanned cow-hides, known as the East India tanned kips from the Madras and Bombay tanneries. The value of these kips for making the 'uppers' for the army boots was realised during the War and Government assumed complete control of the trade purchasing in India the whole of the available supply for export direct to the British War Office. Whereas 194,763 cwts. of tanned hides valued at Rs. 1.75 crores were exported in 1913, in 1917-18, 361,674 cwts. valued at Rs. 4.86 crores were exported. In addition to the export trade in East India kips, Indian tanneries produced, during the war period, greatly increased quantities of leather accoutrements of all sorts and boots for the army in India and the Indian expeditionary forces. Thus the Government under the direction of the Munitions Board gave a great stimulus to the tanning industry and the output of the annually produced boots and shoes was twenty times bigger at the end of the War than before it. Under the system of priority certificates the Munitions Board endeavoured further to stimulate the manufacture in India of certain classes of leather goods previously imported from abroad, such as roller skins, picker bands, leather belting and the raw hide pickers required by the textile mills.*

The Chrome process of tanning which enables superior leather to be produced, has made very slow progress in India, though

* Industrial Hand Book, pp 160-168.

it was thoroughly well established in America by about 1895. The Government of Madras did valuable pioneering work from 1903 to 1911 to demonstrate that chrome tanning could be successfully established in this country. It is, however, to be regretted that the Government had to sell the factory in response to protests from the Upper India and Madras Chambers of Commerce who raised the cry that private trade was invaded. Since the outbreak of the War, however, progress has been more rapid. Indian chrome leather hides found a profitable market in Great Britain. There are several difficulties experienced in connection with the development of chrome tanning in India, such as the highly technical processes requiring chemical knowledge and costly equipment of machinery. A considerable proportion of the Indian cow-hides and goat skins is, however, eminently suited to this class of work and promising developments may be expected under the guidance of the expert tanner whose services have been secured by Government for the development of the tanning industry.

§ 13. Protection to the industry :—The Government of India introduced a Bill in the September session of the Imperial Legislative Council of 1919, to amend the Indian Tariff Act, 1894, so as to levy an export duty of 15 per cent on hides and skins with a rebate of 10 per cent on hides and skins exported to other parts of the Empire and actually tanned there. The duty was imposed as a measure of protection to the Indian tanning industry which had received a great stimulus from the Government patronage during the war but which was likely to dwindle with the fall in military needs unless some other support was given to it. As the Indian tanneries, however, could only deal with a small proportion of the total supply of hides and skins in the country, the rebate was justified as a measure of help to the tanning industry within the Empire, so as to divert the tanning of Indian hides from Germany to the British Empire. The experiment, however, failed to achieve either of the objects. The Indian Tanning industry did not succeed as was expected. There was a fall in the export of hides from India to half the pre-War level and the greater part of the trade again passed to Germany. The Fiscal Commission condemned the duty as wrong in principle, on the

ground that if protection was needed, it should be given through an import and not an export duty. The Government of India, impressed with the defects of the duty, reduced the rate to 5 per cent and abolished the 10 per cent rebate in 1923, the retention of the 5 per cent duty being justified on the ground of revenue need. The Majority of the Taxation Enquiry Committee, however, agreeing with the Fiscal Commission advised its early abolition. Dr. Paranjpye and Sardar Jogendrasingh held that the experience of the last few years was not conclusive owing to the abnormal conditions of the War and advocated a determined policy of protection for the Indian Tanning industry and the retention of the export duty. The Taxation Committee, however, recommended the retention of the duty on skins which enjoy a good reputation in the world market and were not injuriously affected by the duty. Accordingly, the Finance Member proposed the abolition of the 5 per cent export duty on raw hides in the Finance Bill of 1927. The Assembly, however, rejected the proposal, to the great disappointment of the exporters, as it was of the opinion that the interests of the Indian tanning industry would be injured by such a course.*

The claims for protection of the Indian tanning and leather manufacturing industry as a key industry deserve to be considered by the Tariff Board. Alongside of protection, however, there is considerable scope yet for internal improvement; for the principal difficulty which the industry has to face is the lack of organisation and expert skill. Two factors have, however, operated in favour of the tanning industry in India in recent years. There has been a noticeable increase in the consumption of leather, particularly for foot-wear, water bags, harnesses etc. Secondly, with the increased consumption of meat in Central Europe there is a considerable supply of domestic hides at prices so low that there is little inducement for Indian hides being exported. This has made it possible for the Indian tanners to select hides and still pay for them prices higher than those ruling in Europe.†

§ 14. Chemical Industries:—"In a modern state the development of chemical industries on a scale that renders them an

* See Review of Trade, 1926-27, p. 90.

† India in 1925-26, p. 312.

important factor in the economic life of the State—as they are in England, Germany and America—necessitates the provision of certain essentials at sufficiently low rates.”* These essentials are first, the fundamental heavy chemicals, especially sulphuric and hydrochloric acids, lime, caustic soda, sodium carbonate, nitric acid etc. These are essential because they are used in the production of other chemicals from indigenous sources and also for the refining of the various natural products or of materials derived from such products. Thus large quantities of sulphuric acid and alkali are required for refining fixed and mineral oils. The other two essentials are (i) fuel for power, heating purposes and metallurgical operations; and (ii) chemical plant.

Though the War gave a considerable stimulus to many of the chemical industries, India still largely depends upon foreign chemicals. Thus in 1926–27, she imported chemicals of the value of Rs. 2·4 crores. Owing however to the great variety and the relatively small quantities of each kind consumed in India, under peace conditions, local manufactures have so far confined their attention to a few heavy chemicals which are largely in demand, the heavy sea freights on acids serving as protection. Simple extracts and drugs are also manufactured on a small scale. Under the pressure exerted by War conditions several chemicals were produced in the country, and it was thus demonstrated that India has many of the essentials necessary to build up her chemical industries.

India's sources of raw materials for heavy chemicals are not deficient if only the various mineral ores are properly treated. Her varied mineral wealth in sulphide ores, saltpetre, alum salts, limestone, magnesium etc. has been already indicated.† Striking success has been already achieved in the manufacture of *sulphuric acid*, which is a most important key industry for all chemical industries, so much so that that its production is suggested as a test for judging the wealth of a country. There was a large demand for it, especially during the war, for explo-

* Industrial Handbook, p 58.

† See Ch. II. Vol. I above.

sives. The industry is already established in India and its future is promising as it has been decided to work up at Singbhum the Burmese zinc concentrates for the production of spelter (zinc). Nitric acid is also now made in India in sufficient quantities to meet the demand and imports are small. The establishment of a plant for the recovery of the by-products in coking, such as tar and ammonia has recently been undertaken.

The other essentials of chemical industries are fuel and plant. The fuel situation has been examined already and it has been shown how Indian coal deposits are unevenly distributed. Coal as fuel is for instance cheap in Bengal which is, therefore, a convenient centre for certain chemical industries; not so South India, however. India's hydro-electric schemes are not as developed as those in Europe and America. Further attempts are necessary to supply cheap electric power for the development of electro-metallurgical and electro-chemical industries. The special plant required by the chemical industries was imported before the War, but much of the simpler plant can be locally manufactured and a start has already been made in this direction.

The most suitable lines of development would be in connection with those industries which make use of the Indian grown raw materials now exported to other countries for being worked into finished products, such as oil-seeds, spices, scents and sandalwood and various mineral products such as manganese, zinc ores etc.

We may in this connection say something regarding the *oil-milling industry*. Though India produces a variety of oil-seeds she is mainly a seed-exporting country and has not properly developed the manufacture of finished products such as refined oils and oil-seed cakes. In Europe and America efficient plant and improved processes have been in use for this purpose. In India we still do our oil-pressing mostly by the archaic method of the bullock and the *ghani* which leaves a large percentage of oil in the cakes thus impairing their usefulness for the purpose of cattle feeding or as fertilisers. In addition to this the oil is usually highly coloured and impure and fetches comparatively low price in the market.*

There has been in recent years a great increase in the number of oil-mills worked by steam or other mechanical power, especially in the case of mustard oil, castor oil and groundnut oil. There are several difficulties experienced by the oil-milling industry in India. In the first place, oil-seeds are admitted duty free into most countries, whereas finished products are subjected to a tariff duty. Secondly, freight on seed is lower than on oil and even cakes. Moreover, the Indian cultivator is prejudiced against machine-made cakes as cattle food or manure. Lastly, India cannot absorb today all the cakes or meal manufactured for fertilisers and feeding though her interests require an increase in this demand.* It is, however, both unsound and uneconomic for India to export her oil-seeds instead of manufacturing the oils and oil-cakes herself. She is thereby deprived of the manufacturer's profits, and Indian agriculture of cattle food and manure of high value. Moreover, vegetable oils have several important uses and play a great part in the economic life of a civilised community. Vegetable oils and tallow are necessary for the manufacture of soap, glycerine, for culinary and lubricating purposes, etc. Since the War considerable attention has been given to the possibility of developing the Indian oil-milling industry on a large scale. Persistent effort to place the industry on a sound footing has every chance of being crowned with success.

§ 15. Paper-making:—The production of machine-made paper in India in modern times apparently dates from 1870 when the Bally Mills were established on the Hooghly. Its neighbourhood is still the principal centre of the industry. The Titagarh Paper Mills were established in 1882 which absorbed in 1903 the Imperial Paper Mill, which had been started at Kankinara in 1892-94. The Bally Mills after an apparently promising career for some years were liquidated in 1905. For 30 years after 1892 no new paper mill was established on the Hooghly, but in 1922, the Indian Paper Pulp Company, which was formed in 1918 for the production of pulp and paper from bamboo commenced manufacture of paper in the Naihati Mill. As regards the up-country paper mills, the oldest of them, the Upper India Couper Mill, was esta-

* Indian Year Book, p. 708.

blished at Lucknow in 1879. In 1885 the Deccan Paper Mill Company was formed and started work at Poona in 1887. After going on for a number of years it ceased work in 1924 owing to depression in the trade. The most important up-country paper mill at present is at Raniganj being started in 1891 by the Bengal Paper Mill Company formed in 1889. There are three other small paper mills in India, two at Bombay and one at Punalur in the Travancore State. In 1927-28, the Karnatak Paper Mills started operations at Rajmahendry for making paper from paddy, straw and bamboo. The Punjab Paper Mills Company has obtained a large concession of *bhabbar* grass in the Punjab for its factory near Saharanpur. Barring these two new mills, the full annual capacity of the old nine mills was placed by the Tariff Board at 33,000 tons, which would be raised to 43,000 tons if the new mills are included. In Assam, a new company has been formed and at Chittagong, a new factory for manufacturing paper pulp from bamboos has been opened.* The Indian production of paper was 32,144 tons in 1926. The Tariff Board estimated the market open to the Indian paper-maker at the present rate of consumption at about 50,000 tons. Thus when the full production is attained by the existing mills they would be supplying four-fifths of the whole demand and, therefore, the market which the Indian mills can capture is not large enough to admit of any great development of the industry. Until the demand in India for finer and more expensive paper increases substantially, no Indian mill will be able to compete with the European mills which specialise in the finer qualities.

The staple material of the paper-maker in India has hitherto been *sabai* grass which grows abundantly in Northern India and is like the Esparto grass in Europe. Indian wood has not yet been used to make paper, and pulp is imported from Europe. For the cheaper kinds of paper rags, hemp, jute waste and waste paper are used. The Indian Paper Pulp Company is a notable exception and makes paper from bamboo pulp. *Sabai* grass grows in scattered tufts intermixed with other vegetation and is affected by unfavourable seasons. The yield of bamboo per acre is larger

* Indian Year Book, 1928, p. 602.

than of grasses and the cost of production also smaller. Bamboo is available easily in Burma, Bengal and South-West India. For the great bulk of the paper consumed in India, bamboo fibre is quite good enough, though as a paper-making material bamboo is inferior to *sabai* grass in strength and durability. But as already pointed out, the Indian demand for the better qualities of paper is small. Bamboo has been the subject of a good deal of attention from this point of view since 1875. In 1905 the possibilities in Burma were investigated by a special expert, and a pulp expert was appointed subsequently at the Forest Research Institute. As a result of the researches carried out there great expectations have been raised regarding the future of the bamboo paper pulp industry, and it is believed that, if the Indian bamboo and grasses could be successfully utilised for paper pulp, the anxiety regarding the world's shortage of paper could be largely removed.

§ 16. Protection to Paper:—The Tariff Board was asked to consider the claim to protection made on behalf of the Paper and Paper Pulp industry in April 1924. The Board excluded certain kinds of paper such as newsprint, pasteboard etc. from the scope of its inquiry on the ground that they did not compete with the product manufactured by Indian mills who could not possibly supply them. The Board's investigation, however, justified the hope that the manufacture of paper pulp and paper from bamboo could be successfully developed in India. They recommended a protective duty of one anna per pound for five years on certain classes of writing and printing paper competing with Indian paper and a loan or guarantee in respect of both principal and interest of Rs.10 lakhs to the Indian Paper Pulp Company at Naihati to enable them to purchase more plant and so test the sulphite process on a commercial basis and the grant of similar assistance to any mill which was prepared to test the soda process. So far as the manufacture of paper from *sabai* grass was concerned the Board did not grant the claim for protection on the ground that it would not prove a commercial success in view of the difficulty regarding adequate supplies of raw material and of fuel in the same vicinity, and that the mills

using this process could not dispense with protection once it was given to them.

Government accepted the first recommendation of the Board and a Bill was introduced and passed in the September session (1925) providing for the imposition, until 31st March 1932, of a protective duty of one anna per pound as proposed by the Board. They extended the period of protection to seven years so as to secure a firm basis for the industry. They did not, however, accept the proposal of the Board regarding loans etc., being impressed by the fact that financial assistance of this sort could not be given to the industry as a whole, but would in fact place individual firms at an advantage in relation to their competitors. Moreover, the privilege of monopoly attached to the patent rights of the soda and sulphite processes precluded the grant of assistance which could only be given to the owners of these rights.* It is unfortunate that Government could not see their way to granting the financial assistance recommended by the Board.

§ 17. Glass Manufacture.—Glass-making is a very ancient industry and reference is made to it by Pliny who speaks of the the superior 'Indian glass' made from crystals. However, no traces survive of the ancient industry, and all that is certain is that in the 16th century it existed as an established industry and had not advanced beyond the stage of producing very inferior material utilised for the manufacture of bangles and to a small extent for small bottles and flasks. Then as now there was a large demand for bangles in the country. Very recently, between 1892 and 1893, five glass factories of the modern type were established, but went out of action sooner or later. Those started under European management struggled hard and survived longer but the last of them failed in 1908. Another unsuccessful European attempt was made in Madras in 1909.

The glass industry, however, seems to have a peculiar fascination for Indians, for, in spite of the previous failures, as many as 16 factories on a small scale were started during the *Swadeshi* period 1906-13, and were the products of purely Indian enter-

* India in 1925-26, p. 297.

prise. In some cases European trained glass workers assisted them and in others they relied on Japanese workers under the control of Indians who had been to Japan to learn the methods. Only three of these factories, however, were in operation on the eve of the war, and none of them was making a commercial profit, though the Talegaon factory in the Poona district, aided by the *Paisa Fund*, was paying its way on the somewhat peculiar and non-commercial lines on which it was run.*

Two well-defined classes of the industry in its present stage can be distinguished; (a) the indigenous cottage (bangle-making) industry and (b) the modern factory industry. The indigenous industry is spread all over India but is chiefly concentrated in the Firozabad district of the United Provinces and the Belgaum district in the South. There is a large colony of bangle-makers and about 60 factories for this purpose in Firozabad. The Firozabad industry is mainly engaged in making cheap bangles from glass cakes or blocks made in larger factories. It supplies nearly one-third of the total demand, and was in a flourishing condition during the War period. The 'silk' bangles imported from Japan are, however, a serious rival to the home-made article.†

The factory industry is yet in a condition of infancy and its production is mainly confined to manufacture of lampware and, to a less extent, of bottles and carboys. As a result of the stimulus given during the War-period by the demand for specialised glass passing through the Munitions Board, several factories have with some success turned out glass tubing, flasks, breakers, petri dishes, test-tubes and a few works have been started to meet the demands of scientific laboratories controlled by the Indian Medical Service. Indian factories cannot, however, turn out sheet and plate glass, laboratory or table glass nor artistic glassware, though the Ogale Glass Works in the Aundh State (Bombay) have recently succeeded in producing flower pots of different designs.

§ 18. Imports of glass :—In the pre-War days India imported glass and glassware valued at Rs. 190 lakhs, the principal imports being bangles, beads, false pearls, sheet and plate glass, lamp-

* Industrial Handbook, pp. 261-63.

† The Indian Year Book, 1928, p. 716.

ware, bottles and fials, soda water bottles, tableware etc. Austria and Germany held a predominant position in the trade, their share being 57 per cent of the aggregate imports. During the War, the imports of bangles and lampware decreased and their place was partially taken up by Indian wares. In 1919 the total value of glassware produced in India was estimated at Rs. 40 lakhs. Japan also increased her share enormously from 6 per cent to 71 per cent. In 1926-27, imports were valued at Rs. 2,53 lakhs and mainly came from Japan, the United Kingdom, Germany, Belguim and Czechoslovakia, which shows that the Indian industry is still in a condition of infancy.

In addition to foreign competition other difficulties are inexperienced control, lack of trained men, insufficient supply of essential materials like coal and soda, sand and lime, inadequate finance etc. In 1927 there were 14 glass factories, the chief centres being Bombay, Jubblepore, Allahabad, Naini, Bijhoi, Ambala, Lahore and Calcutta. The choice of sites for the glass-works, especially during the War period when the high prices led to the neglect of this factor, has not always been quite happy and personal considerations rather than convenience in respect of the vicinity of raw materials and markets have often been allowed too much influence. Allahabad and Naini in the United Provinces enjoy enormous advantages over other centres like Bombay owing to their location in the vicinity of raw materials and fuel supplies.

The fuel difficulty may be overcome by the supply of cheap electricity for working electric glass furnances. The labour difficulties are no doubt serious. The glass industry even in its simple form is highly technical and can be efficiently conducted only by scientifically trained managers and expert workmen. It may be noted in this connection that useful work has been done by the Paisa Fund Glassworks at Talegaon in training glass-blowers, and the expansion of the industry under War conditions is chiefly due to the supply of men who have come from this place, though the training given leaves much to be desired. As Sir Alfred Chatterton points out, "the glass industry has come to stay, but, without aid from the state, it is likely to make slow progress in the future." He suggests the establishment

of a Government glass factory equipped with an efficient technological laboratory and a competent staff of experts and skilled glass workers.* Railway facilities are also necessary. In short, it is necessary to examine thoroughly the economics of the glass industry and the question is of sufficient importance to form the subject of inquiry by the Tariff Board.

§ 19. The Cement industry:—It is surprising that in spite of the large home market in India, favourable conditions to manufacture and the national importance of the industry, the cement industry occupied an insignificant position before the War, and was not able to produce cement up to the requirements of the British standard specifications. Even before the War India consumed large quantities of cement importing about 180,000 tons a year. The demand for cement has been increasing since and is now in the neighbourhood of 400,000 tons a year. The use of ferro-concrete in bridges and heavy structural work of all kinds is extending rapidly. It has even been said that the Steel Age is now giving place to the Cement and Ferro-concrete Age.

The manufacture of portland cement commenced in Madras as long ago as 1904.† It was, however, only on the eve of the War that production on a large scale was contemplated in India by the three Companies formed in 1912-13. The earliest to start operations was the Indian Cement Company at Porbunder (Kathiawar) followed by the Katni Cement and Industrial Company (C. P.) and Bundi Portland Cement Company (Rajputana). During the War the industry developed, especially under the patronage of Government who purchased, during the latter part of the War, the great bulk of their output. In the post-War boom period, a number of companies were floated under the temptation of large profits which the industry was then earning. The three old companies doubled their output and seven new ones were projected and six of them started operations by 1923. Thus the development was very rapid and the aggregate production increased from 945 tons in 1914 to 236,746 tons in 1924, the imports showing a decrease

* Industrial Handbook, p. 269

† Tariff Board (Cement Industry) Report.

from 165,723 tons to 124,186 tons during the same year.* The imports have further declined to 101,000 tons in 1926-27.

The Tariff Board found that the industry possessed several natural advantages, such as abundant limestone of excellent quality in many parts of the country and close to railway lines; suitable clay also close to railway lines; and the production of gypsum in the country though it has to be transported over long distances. But the industry labours under a considerable handicap with regard to fuel as most of the works are situated away from the coal fields. Regarding markets, the Board point out that the up-country market is a naturally protected market for the Indian cement works, which, except for the two Kathiawar factories, are above 300 miles from the port. Elsewhere, Indian cement has to face the competition of foreign supplies. However, as the principal market for cement in India is not up-country but in the ports of Bombay and Calcutta, most Indian factories are at a disadvantage here being away from the ports.

The Tariff Board, to whom the claim of the industry for protection was referred in April 1924, declined to recommend protection to the industry on the ground that it was suffering from overproduction and prices were determined by internal competition among the Indian manufacturers and not by the imports. The Board calculated that the Indian works were already capable of supplying a maximum output of 600,000 tons, whereas the annual consumption was only 390,000 tons. They considered, however, that it would not be long before conditions become stable, and with a view to the removal of the handicap to which Indian cement is subject owing to the great distance of most of the factories from the coal fields or the ports, recommended that legislation should be introduced authorising the Government to pay bounties on cement consigned from Indian factories to certain ports or to railway stations within a specified radius of these ports, provided the payment of bounties did not lead to a reduction in the price of Indian cement in relation to the price of imported cement. The Government of India did not accept the principle of such condi-

* Tariff Board (Cement Industry) Report,

tional legislation and decided not to take any action on the report.*

§ 20. Other Inquiries by the Tariff Board :—It is not possible here to describe the growth of all the other industries whose claims for protection have in recent years been investigated by the Tariff Board. We may, however, briefly refer to some of these inquiries. (1) *Printers' Ink* :—During 1924-25, the Board examined the application made by the Hooghly Ink Company, which is the only large firm in India. It was represented on its behalf that while imported printers' ink was subject to a duty of only $2\frac{1}{2}$ per cent *ad valorem*, the Indian manufactures had to pay 15 per cent *ad valorem* duty on the raw materials imported from abroad. Therefore, they claimed either (a) exemption from the 15 per cent duty or (b) that the import duty on ink should be raised to 15 per cent. The Board could not agree to the first alternative on administrative grounds. Regarding the second alternative, the Board found that practically the disability on local manufactures would be removed by increasing the duty on printers' ink from $2\frac{1}{2}$ per cent to 5 per cent. The Government of India gave effect to this proposal in the Tariff (Amendment) Act, 1926. (2) *Magnesium Chloride* :—The Tariff Board declined to recommend protection to the Pioneer Magnesium Works, Bombay, who had represented that they were unable, since the War, to compete with the magnesium chloride imported from Germany, on the ground that the Pioneer Works had failed to show that the Industry would eventually be able to dispense with extraneous assistance. Government of India agreed with this finding. (3) *Coal Industry* :—Reference has already been made to the competition of foreign coal, especially of the South African coal in India and the demand for protection for the Indian coal industry.† The Tariff Board, to whom the question of protection was referred, concluded its inquiry in 1926. It reported that there was no case for general protection, but they considered that a duty at the rate of Rs. 1-8-0 per ton would be justifiable. It held by majority that a countervailing duty on South African coal was

* See India 1925-26, p. 296.

† See Ch. II, Vol above, p 19

inadvisable. Mr. Ginwala dissenting from his colleagues recommended that a countervailing duty of Rs. 1-8-0 per ton in addition to the existing duty of 8 annas per ton, should be imposed on South African coal. The Government of India agreed with the unanimous finding of the Board that the case for a protective duty on all imported coal had not been established, and endorsed the view of the Majority that in the existing circumstances the imposition of such a duty was not advisable.* (4) *Match industry*:- The Board recently issued their report (August, 1928) on the inquiry into the claim for protection made by the Indian Match Industry. We need not enter into the details of the earlier history of the industry. It has shown considerable expansion in recent years as a result of the imposition, in 1922, of an import duty for revenue purposes on matches, of Rs. 1-8-0 per gross, or more than 100 per cent *ad valorem*. The industry commands a large home market, consumption being estimated at 17 million gross a year. Labour is cheap and well able to manipulate the simple machinery. There are at present about 27 factories with a capacity of 500 gross a day or over. The imports of matches have declined from 13.68 million gross in 1921-22 to 6.13 million in 1926-27. The most striking development has been the establishment, in view of the import duty, of match factories in India by the gigantic Swedish Combine, which already controls about 70 per cent of the total world's demand, and there has been considerable agitation by the Indian Chambers of Commerce about the adverse repercussions of this dominant foreign concern on the indigenous industry. Regarding the claim for protection, the Board held that the prices of Indian matches were regulated by internal competition and the consumer got them as cheap as it was possible to get them and that the industry would be able to resist world competition without the assistance of the state. They recommended, however, that the current revenue import duty (Rs. 1-8-0 per gross) should be converted into a protective duty for an indefinite period so as to give assurance to the industry that it would not be deprived suddenly of the protection it has enjoyed so far. They did not how-

* India in 1926-27, p. 191.

ever, recommend any measures for the time being to safeguard Indian interests against the Swedish Match Company in India. They held that the Company had been doing useful work in the expansion of the industry in India, and that with protection for the Indian industry it will help powerfully in developing Indian sources of supply of the raw material and, in general, in enhancing the standard of quality and introducing of modern methods. The Board, however, advised the Swedish Company to adapt itself to Indian nationalist and political sensitiveness by reconstructing itself with a rupee capital and admitting Indian Directors, and admitted the necessity of keeping a watch on the Company to see to it that it did not employ its large resources to establish a monopoly in India.*

The Assembly in its September session (1928) passed the Match Industry Protection Bill as recommended by the Tariff Board. A considerable section of public opinion in the country along with the Indian Chambers of Commerce was strongly opposed to the policy of the Tariff Board and Government in allowing a foreign concern like the Swedish Company to avail itself of the advantage of protection without the statutory adoption of the usual precautions to safeguard Indian interests. Government assured the Assembly, however, that they would certainly take special precautions to see that the Swedish Combine did not prove a menace to the indigenous industry by developing into a monopolistic concern. They also announced that they did not contemplate keeping for long the protective duty at its present height.¶ (5 *The Petroleum Oil Industry*:-The Tariff Board recently (September, 1928) issued their report on the claim for protection made by the Indian Petroleum Industry who had represented to the Government of India that the indigenous industry was hit hard by the Kerosine oil rate war between the Standard Oil Company of New York and the Royal Dutch-Shell group, resulting in the

* The Board held that it was utterly impossible to build up a cottage match-making industry in India, in view of the competition of the mass production of factories. See Tariff Board's (Match Industry) Report, 1928, pp. 100-104.

¶ The Times of India, 15th September 1928.

dumping of kerosine oil in India at prices below world parity. The immediate cause of the war was said to have been the purchase by the Standard Oil Company of New York from the Soviet Government of Russia of kerosine, which the Royal Dutch Shell Group claimed as rightfully belonging, at least in part, to them. The Majority of the Board, while admitting that the sale of imported oil at prices below world parity had been established,* held that the applicant companies had failed to prove their claim for protection and to disclose certain facts regarding the offer of compensation by the Dutch Companies for losses suffered by the former as a result of the oil war. Moreover, the oil war was not opposed to national interests and was an incentive to progress in the Indian industry. The Government of India agreeing with the Board declined to take any steps to protect the indigenous industry, especially as the rate war had ended.

COTTAGE INDUSTRIES.

§ 21. Causes of the persistence of small-scale production :— Industrial advance at the present time is generally associated with the predominance of production on a large scale. It must be remembered, however, that it does not necessarily bring about the total extinction of small-scale industry. Even in modern factory production, there are of course limits beyond which it is not advantageous to increase the scale of production. The most effective scale of production is a matter which to some extent depends on the kind of motive power used. The increasing use of electricity instead of steam would, for example, tend to make the unit of production smaller than the average factory at present without involving any sacrifice of important external and internal economies. Again, most text-books on Economics are careful to mention that in every progressive society there are a number of articles, e. g., artistic products and many luxury goods which do not lend themselves to standardised production. Further, many of the improvements in the material equipment of civilisation give rise to a number of small establishments to keep them going. An illustration that readily comes to mind is the multi-

* The President dissented from this view.

plication of workshops for mechanical repairs which come in the wake of any considerable development of motor transport. Finally, new industries, so long as they are in an experimental stage, are first tried on a small scale and it is only when their success is demonstrated that they are organised on a large scale.* It thus comes about that even in the most advanced countries of the West, a number of small industries exist and flourish side by side with large-scale industries. For example, in France more than 99 per cent of the industrial establishments employ less than 100 workmen each and of these the great majority employ less than 50 workers each. It is interesting to observe that, even in England, the home of large-scale industry, as many as 36,000 factories and workshops employed not more than five workers apiece in 1897, and even as late as in 1913, in the majority of trades the number of employees per establishment was below 20.†

§ 22. Industrialisation and Cottage Industries in India:—In India, under the present conditions, industrial undertakings on a small scale have great possibilities and industrial expansion in the near future is likely to be marked by the multiplication of small-scale enterprises all over the country. We have seen that even in modern industrial countries there is always room for the small industry. In modern industrial development, particularly in India, the persistence of small-scale production will be a feature of industrial expansion. This is, however, a different thing from saying that India's progress in industrialisation in the modern sense of the term will leave all the industries of the old type intact and in undiminished vigour. Such a statement would be so palpably false that it does not stand in need of refutation. *Some old extinguished industries will almost always lie about the cradles of new-born modern industries, and we must expect that intense industrialisation will be injurious to some of the handicrafts which exist at present.* In some cases, the disappearance of old handicrafts may be unavoidable and must be accepted as the price of industrial progress, though it is to be desired that every effort should be made to minimise the suffering and demoralisation attendant

* Mukerjee : *The Foundations of Indian Economics*, p. 360.

† *Economic Journal*, Dec. 1922, pp. 489-90.

upon the transition and to ease the passage of inevitable change by making it gradual and by assisting those adversely affected by it to find a suitable alternative employment and in other ways. A brief account has already been given of the manner in which the economic transition in India has affected the various indigenous industries,* and it has been pointed out that the artisans were left to their own resources and had to meet the new situation as best they could without any sort of guidance or help from the state. This was a mistake and care should be taken not to repeat it in future. Some of the old industries like hand-spinning have already succumbed, and we do not believe that the country is likely to gain by attempts to resuscitate it by artificial means, though we have already admitted that as an ancillary occupation to agriculture it has some small possibilities. There are other cottage industries whose products are competing directly with machine-made goods and which may be described as being in a state of suspended animation. Those who cling to them do so because of their unwillingness to give up their hereditary occupation, or because they are deterred by the hard conditions of factory work as at present organised, or because they may be forced to remain in their traditional vocation by "the patron and incubus" of the petty artisan in India—the merchant financier, who is interested in keeping him there indefinitely, so that he may recover his money and continue to exploit him. Each of these cases suggests its own appropriate remedy. Sheer conservatism must be overcome by propaganda and education which should teach the artisan quickly to adapt himself to changed circumstances. The dread of factory work must be removed by improving the lot of the factory worker and making conditions of work in the cities less deterrent than they happen to be at present. Emancipation from indebtedness must be effected by co-operative credit and other methods already discussed.* The third category is that of cottage industries which do not suffer from inherent and irremediable weakness like the first two classes just noticed and may be fit to survive even under modern conditions. Those industries, for example, which

* See Vol I, Chap V, Sections 20, 21, and pp. 176-178.

† See Chapters IX and X, Vol. I.

are closely connected with agriculture and which require simple tools have generally nothing to fear from factory goods. There are also cases where the artisans have successfully adapted themselves to the new conditions and learnt to use superior raw materials and better tools. "The weaver has taken to mill yarn, the dyer to synthetic dyes, the brass and copper-smith to sheet metal, the blacksmith to iron rolled in convenient sections, in each case with advantage to himself from the lessened cost of production, which has greatly extended his market. In some districts in lower Bengal, the weavers use the fly-shuttle slay extensively; and they have recently adopted it in large numbers in the coast districts of the Madras Presidency; while it is also gradually coming into use elsewhere. The tailors invariably employ sewing machines, and town artisans readily take to improved tools of European or American manufacture."* Again, the economic strength of some of the handicraftsmen is due to the fact that the goods they turn out are of such a character that they allow no scope for the employment of automatic machinery and large-scale production, or are not any cheaper or better for being machine-made rather than hand-made. Again, popular taste may require too great a variety for the goods to be profitably turned out on a large scale by means of modern mechanical appliances. Proximity of the market, and a more intimate knowledge of the consumers' wants may further turn the scale in favour of the cottage worker.† Further, the self-sufficiency of the village though no longer preserved in its entirety is not altogether a thing of the past even now, particularly where the railway has not yet penetrated, and consequently some of the artisans still continue to occupy their old recognised place in the corporate organisation of the village and

* Industrial Commission's Report, pp. 193-194.

† "Thus some kinds of head-wear, *dhotis* and *saris* made by the handloom weavers have not been displaced by modern factories. The weavers of Dacca, Murshidabad, Madura and Benares, those engaged in making embroideries in Lucknow and Delhi and lace in Surat supply commodities for which the demand in the country has not been seriously affected by competition with similar machine-made articles. The metal worker, the shoe-maker, the goldsmith, the tailor, the confectioner and other craftsmen fall into the same category and are similarly protected." *India in 1926-27*, p. 330.

serve the simpler needs of the village-folk as in the days of yore receiving their remuneration in the manner already described.* However, the self-sufficiency of the village is being invaded more and more and as it disappears the position of these artisans will need to be readjusted.

Modern industry has made but little head-way in this country so far, and the policy of free imports of cheap foreign manufactures in spite of its far-reaching economic consequences for the country has by no means yet wrought the complete destruction of all the indigenous industries, so that the number of people engaged in small unorganised enterprises is still very large.† And while striving for rapid industrial expansion we must watch it with reference to its effects on the welfare of the numerous humble artisans throughout the country.

We may repeat that this does not imply that the State should try to perpetuate the existence of all old industries whatsoever at any cost, but it does suggest a thorough investigation of the position of each cottage industry in view of the prospect in the near future of substantial progress towards industrialisation. Where it appears that an old industry is doomed to extinction, it is the part of wisdom to accept the inevitable and the problem in this case would be that of securing a painless euthanasia. Where, however, an industry of the old type possesses elements of inherent vitality, its survival should be assisted by every possible means. If large-scale organisation is the essential condition of industrial progress we must accept it unhesitatingly while guarding against its peculiar evils and dangers. But it is obvious that *where organisation of the old type does not spell economic stagnation or weakness its continued prosperity should be the object of our solicitude.* The Cottage Industry secures a happier existence for the craftsman who

* See Vol I, Chap. V.

† "We have been unable to obtain accurate statistics regarding the actual number of workers in the various cottage industries, but in every town they still form a large percentage of the population, and they are to be found almost in every village, so that their numbers are still vastly larger than those of the operatives employed in organised industries." *Industrial Commission's Report* p. 194.

works under comparatively healthy conditions in his own home in the midst of his family. Understanding as he does the whole series of connections between the making and the using of the articles he produces, he can take much greater interest in his work and is able to enjoy something of the pleasure of artistic creation. It is also clear that in the cottage industry with its autonomous worker, there is no place for any antagonism between the employers and the employed, the possibility of which constitutes an ever-present difficulty of modern industry.

In the light of these remarks we shall now proceed to examine briefly the present position of some of the cottage industries in India, and for this purpose we shall select the textile industries which are by far the most important and the widest in extent in India.*

§ 23. The Cotton Handloom Industry:—Hand-spinning of cotton is now almost completely extinguished and it need not detain us.† Hand-weaving, however, still provides subsistence to nearly six millions of people. The Industrial Commission estimated that between two and three million handlooms are at work in India with annual gross earnings of about Rs. 50 crores. And though it is no longer true that "everyone from the Cape of Good Hope to China, man and woman, is clothed from hand to foot in the product of Indian looms," (Pyrard), and though the present position of the industry is far from satisfactory it has a great future before it, if suitable measures are taken properly to organise it.

There is no gainsaying the fact that handloom weaving has suffered—and in some cases suffered severely—on account of the competition of mill-made goods and the weaver has had no chance of success when pitted against large-scale organisation turning out exactly identical articles at a much smaller cost.

* While, among the textiles we have dealt with cotton, wool, and silk in this connection, we have omitted jute for the reason that as a cottage industry jute manufactures have no future before them, the goods turned out being of a kind that are far more economically manufactured by machinery than by the hand-loom.

† We have already discussed the possibility of the revival of the Char-kha in Section 19, Chap. V, Vol I.

Under these circumstances, the weaver has had to abandon his calling in favour of agriculture, joining the ranks of landless labourers, or has been forced to lead a very precarious existence with even less power of resistance against famine and scarcity than an ordinary cultivator. His position is, however, stronger in the case of goods which are either too coarse or too refined and artistic and as regards which the handloom can hold its own against machinery. The poorer classes, especially the villagers, prefer the handloom cloth as it is supposed to be stronger and more durable than anything of the same kind produced by the mills. The mills cannot take up the manufacture of the large number of specialised types of cloth, the use of which is decreed by the slow-moving Indian custom, because although the demand in the aggregate is large, the demand for each type is too small to make its manufacture in a factory economically worth considering. There is, of course, also the case of the finest fabrics of genuine artistic excellence where individual skill is required. There is thus a clearly demarcated field where the handicraftsman remains supreme and which cannot be usurped by the factory.

The weaver working in his own home works longer hours than the factory labourer, and has also the advantage of unpaid assistance from the women in the family in the intervals of domestic work. The hand weaver is moreover content with a very small margin of profits as his standard of comfort is low. While this is a factor which increases his competitive power, its existence is not a matter for congratulation. The aim of reform ought to be so to improve the efficiency of the handworker as to enable him to adopt a higher standard of life. Even a superficial investigation into the condition of the handloom weaver reveals the fact, that although there are sound economic reasons for hoping that he ought to prosper if he confines himself to his proper sphere of work where the factory cannot trench on his dominion, his actual position is one of extreme poverty and distress. The discussion of the causes of and remedies for this state of things is capable of a generalised treatment applicable to all

the cottage industries and has been placed at the end of the Chapter.

§ 24. Woollen Industry:—The manufacture of woollen goods in some shape or form is found in all parts of the country for the simple reason that the sheep is a ubiquitous animal, though the quality of the wool varies from place to place, the sheep in the hilly tracts generally yielding wool of finer quality than those in the plains.

Under the Mughals the manufacture of woollen carpets had reached a high pitch of excellence. The demand for woollen carpets came mainly from the royal courts and the nobility, and the industry found its natural habitat in the principal capital cities, though it migrated to other centres on the break-up of the Mughal Empire. The downfall of this Empire practically extinguished the local demand for carpets, but it was gradually replaced by foreign demand after the establishment of British rule. The foreign demand, however, although it helped to stay the economic ruin of the artisans, was responsible for a deterioration of the quality of the goods. It encouraged the production of cheap articles fashioned according to patterns sent out to India from abroad. The growing use of aniline dyes was a further cause of deterioration. The opening of the foreign markets also led to the appearance of a large number of middlemen which is the characteristic feature of trade in modern India, especially of the export trade. Carpet-weaving in India at the present time depends almost entirely on foreign demand which absorbs as much as 90 per cent of the total production.

The carpet weavers were mostly Mahommedans who organised themselves into caste guilds which controlled the wages of workers and the prices as well as the quality of the goods produced. The guilds seemed to have functioned effectively and exercised a salutary influence on the industry. In course of time however, the guild organisation suffered disintegration. Also, the craft ceased to be the monopoly of Mahommedans and has come to be practised by a small number of Hindus as well, who often combine it with agriculture. About fifty years ago, carpet-weaving was introduced into the jails, and the convicts trained in

them often found employment in factories started at different places by exporting firms.

Considered as a cottage industry, carpet-weaving is in a languishing condition on account of the ignorance and poverty of the weaver and the absence of organisation. It is usual for the weaver to accept advances of money from the dealer, and the system of advances tends to convert the independent handicraftsman into a bond slave of the dealer and destroys personal interest in the work on the part of the weaver and all incentive for improvement. He is not able to take his labour or goods to the best possible market but must work according to the dictation of the dealer.

The manufacture of shawls had attained great renown in India in the pre-British days, especially in Kashmir, and the Mughals were particularly interested in its development. For example, it was due to the efforts and patronage of Akbar that the industry came to be established at other centres than Kashmir, such as Amritsar, Lahore, Ludhiana etc. The shawls of Kashmir were unrivalled for softness and fineness of texture and were in great demand in the countries across the frontier and in Russia. The famine of 1830 dealt a severe blow to the industry from which it never quite recovered and its difficulties were enhanced by the numerous imposts to which it was subjected in the Kashmir State. The development of an export trade to Europe which began in the early years of the 19th century was helpful in arresting the decline of the industry and is supposed to have at one time provided employment for over 15,000 workers. The Franco-German war of 1871, however, was responsible for an abrupt shrinkage of the European demand. Nor was this sudden check temporary in character, for shawls rapidly went out of fashion in Europe and in spite of the close of the war no revival was experienced by the trade. Another important factor which contributed to this result was the starting of shawl manufacture at Paisley in England. The sale of the famous Paisley shawls at one time exceeded a million pounds and they successfully ousted the Indian article from the European markets.

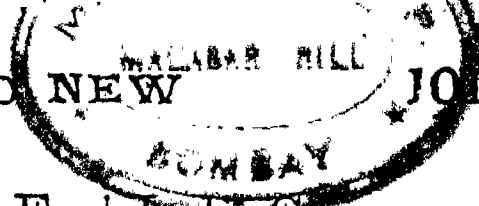
Another woollen manufacture that is widely prevalent in the

country is that of the coarse rough blanket (*kambli*), which is put to such a variety of uses by the humble folk in the villages and "serves as bed, portmanteau, overcoat or umbrella." The production of blankets is generally a by-occupation pursued by shepherds or agriculturists who are mostly Hindus. There is no export trade in these articles but the industry is nevertheless important because a very large number of people are engaged in it. It is immune from the competition of machine-made goods because the latter cannot stand the rough wear to which the *kambli* is subjected. Having regard to the facility with which the raw material can be obtained in every part of the country and the largeness of the home market, blanket-weaving would appear to hold out great promise as a cottage industry and its possibilities need to be systematically explored.

§ 25. Sericulture and silk manufactures:—The last set of textile cottage industries to be noticed are those connected with silk.

The production of raw silk or sericulture "concerns itself with the rearing of silk-worms under artificial or domesticated conditions, their feeding, the formation of cocoons, the securing of these before they are injured and pierced by the moths, and the maturing of a sufficient number of moths to supply eggs for cultivation of the following year." The first essential is an adequate stock of mulberry trees for feeding the worms in their larval stage. The soil in which the mulberry grows, and the age and condition of the trees are important factors governing the successful practice of sericulture. An abundant and cheap labour supply is another indispensable factor. Whatever success sericulture has achieved in India has been confined to those parts of the country like Bengal, Kashmir and Mysore where all these conditions are found to be present.

Roughly, during the first three quarters of the 17th century the East India Company was primarily interested in the trade in raw silk. Subsequently the Company realised that greater profits were to be made by exporting Indian silk manufactures to England and they pursued this policy with sufficient vigor and success to alarm weavers in England. Owing to the opposition



of English weavers and for other reasons, the East India Company once more reverted to the trade in raw silk and suffered heavy losses in the process, which compelled it to withdraw from active participation in the trade after 1835. In the meanwhile, the policy of favouring the production of raw silk and discouraging that of manufactures had an adverse influence on the indigenous weaving industry* whose position was further worsened by causes similar to those referred to in explanation of the decline of the woollen manufactures of carpets and shawls, viz, a change in the nature of the European demand and the progress of silk weaving in Europe which soon outstripped the Indian industry as regards technique. To this list of causes must be added the emergence of Japan, China and the United States as competitors in the European markets, and as regards the local market, the demand for the kind of goods produced on the handloom was diminishing among the educated and well-to-do classes who might have been expected to fill, but did not fill, the void created by the extinction of the old nobility and the royal courts.

In short, both sericulture and silk-weaving have suffered in India in recent times. India's exports of the raw material have not only decreased in volume but they have also changed in form. Most of the silk exported at present is in the form of waste or cocoons. The reeling is so badly done in India that foreign countries prefer to take the cocoons from this country and do the reeling themselves. The same reason explains the increasing popularity of imported silk in India. The Indian weavers themselves prefer the more even re-reeled Chinese or Japanese to the home-made product which is "full of knots and loose ends and of unequal strength." Efforts are being made, especially in Bengal, to improve the quality of the Indian silk. The Agricultural Department in that Province runs two sericultural schools. A large number of seed farms have also been started and are managed under departmental supervision by students who have completed their course at one of the schools. The students trained at these schools are given awards of Rs. 250 each and are provid-

* The decline of the silk industry is indicated in a striking manner by figures for the export trade. The value of the export of silk in 1836 was Rs. 3,296,000; in 1925 it amounted only to Rs. 295, 000.

ed with 'seed stocks' from Government nurseries for erecting rearing houses. This is known as the Selected Rearing System and is showing good results. Apart from Government interest in silk production displayed in this manner, a further stimulus is incidentally provided by the high revenue duty of 15 per cent on imports of foreign silk. We have already said, however, that as recommended by the Textile Tariff Board, the duty on imported artificial silk was reduced from 15 to $7\frac{1}{2}$ per cent in 1927. As to the silk weaving, the indigenous industry has been steadily losing ground to manufactures from abroad for want of efficient organisation, the hopelessly inadequate resources of the average weaver and his antiquated methods of production. The manufacture of silk goods as a cottage industry enjoys certain exceptional advantages under the existing circumstances in India. Large-scale production with modern mechanical appliances is relatively more difficult than in the case of cotton manufactures and has hardly yet made a beginning in this country. In any case, silk manufactures being largely of the nature of luxury goods in India admit of a great diversity in workmanship, so that a large sphere of operations will always remain which the handloom alone can occupy. As regards imports of finished goods from abroad, the home industry is sheltered in a large measure by the import duty on manufactured goods which is twice as high as in the case of the raw material. Lastly, there has been in recent years the growth of a well-marked tendency on the part of Indians to extend a patriotic preference to indigenous as against foreign goods. Circumstances would thus seem to be peculiarly propitious at present for reviving the silk cottage industry.¶

§ 26. Methods of aid to cottage industries* :—A careful investigation into the possibilities of cottage industries in India will tell us which of them are likely to flourish. But merely making sure that some of them are fit to survive and prosper, will not help them to do so. The ignorance and poverty of the small artisan together with the absence of any effective organisation for directing his footsteps into the proper path, make it

¶ For a fuller discussion of the textile cottage industries see P.V.Deolalkar : *Textile Industries in India*.

* See India in 1926-27, pp 330-338.

necessary that a comprehensive scheme for assisting him must be elaborated and put into operation. The first obvious step, of course, is *better general education* which should make some attempt to provide *manual training and instruction in industrial crafts*. Over and above this, sufficient provision for the education of the artisan in *special industrial schools*, preferably controlled by the Director of Industries, is necessary. In Bombay, the Department maintains six weaving schools for the benefit of the hand-loom weavers. The Industrial Commission also recommended that for the training of the more intelligent of the artisan population to enable them to be master-workers, *demonstration handloom factories* assisted by the Government should be started and a commercial section should be attached to the weaving schools, so that the more enterprising artisans so trained may be fitted to start small handloom factories on their own account. The jails and reformatory schools make a speciality of teaching various industrial crafts to their inmates such as carpentry, cane and bamboo work etc. with a view to enable the prisoners to set up as craftsmen after they are discharged. Their career, however, after they are released, is not systematically watched and it is difficult to say how far this effort at giving instruction in handicrafts to the prisoners is helping the maintenance of cottage industries. One of the handicaps from which the cottage industries very often suffer is the difficulty of obtaining *cheap raw material of good quality*. The necessity of improving the quality of indigenous cotton and silk, for example, is obvious from this point of view. Another needful reform is *the invention and introduction of more efficient tools and implements*. "In Bihar and Orissa, the Province has been divided into ten circles, each in charge of a demonstrator who conducts peripatetic demonstrations of improved appliances. These parties are based on the Cottage Industries Institute which carries out experiments in its various sections, arranges for the supply of looms, dyes, accessories, etc., and introduces new cloths and new patterns among weavers. Similar services for the silk industry are performed by the Bhagalpur Silk Institute, while the experimental blanket factory at Gaya is attempting to do the same for the primitive blanket industry in the south of the Patna Divi-

sion." † Similar attempts have been set on foot by some of the other Provinces as well. Valuable assistance can also be granted by *giving the artisans new patterns and designs* to work upon so as to increase the sales. In many cases a *better organisation* of production may be possible. There may, for example, be greater scope for division of labour even in simple cottage industries. Bringing the workers together under one roof would give us the factory system in its essentials, though the factory may not be situated in a congested urban area and may not use mechanical power. This form of organisation has been found to be unsuccessful because the independent cottage worker cannot be easily broken in to the factory discipline. Another possible variant is afforded when the workers work in their own homes under the direction of factory managers who undertake the responsibility of financing production and marketing the goods. This system, however, lends itself to exploitation and sweating in a worse form than is possible in a regular factory.

By way of *providing the handicraftsman with the requisite capital* the Industrial Commission suggest that in some cases small loans should be given by the Director of Industries, or tools and plants should be supplied on the hire-purchase system under which these would become eventually the property of the artisans. But the most promising solution of the problem is afforded by *co-operative credit*. This leads us to note that the principle of co-operation is of very fruitful application* for the purpose of bettering the lot of the small artisan, whether by providing loans at a moderate rate of interest or helping him in the purchase of raw materials, tools and implements and in the sale of the finished article. The position is highly unsatisfactory particularly in regard to the marketing organisation. As things stand at present, the artisan fails to get the best price for his goods being unable to advertise his wares properly. The Arts and Crafts Emporium at Lucknow and a similar one at Lahore are intended to remove this handicap to some extent, but such emporia need to be far more numerous to produce any appreciable effect in the desired direction. Much attention is paid in foreign countries

† India in 1926-27, p 333.

* See Vol. I, pp. 354-55 and 361-362.

to the question of developing an efficient marketing organisation. The toy industry of Germany and the cottage industries of Japan owe their success to the existence of the essential business organisation which takes over the produce of the industries and disposes of them within the country as well as abroad. At present the foreign markets are neglected in India and even the home market is not properly nursed. An organisation like the Swadeshi Stores in Bombay is a good example of an active and successful agency for internal distribution of indigenous products and furnishes a type worthy of imitation. The Department of Industries should work in co-operation with a business institution of this sort in order to take the products of Indian handicrafts to customers all over the country and outside. Apart from the creation of such an organisation and the establishment of co-operative societies, a central trading organisation is necessary not only to find the widest possible market for the cottage wares but generally to secure co-ordination and co-operation between the isolated and unrelated cottage industries.*

One often hears complaints about the deterioration of artistic taste among the people of this country including the educated classes. A wide advertisement of artistic indigenous products will not only benefit the handicrafts, but it will also assist the formation of a proper aesthetic taste among the people.

Another way in which Government might help is by extending their patronage to the cottage industries. The Provincial Stores Purchase Department in the United Provinces, for instance, has apparently accepted this policy and buys goods whenever possible from local manufactures.

As welcome signs of increasing state interest in the problem of the regeneration of cottage industries we may refer to the recent legislation passed by some of the provincial Governments, e.g. the State Aid to Industries Acts of Bengal and of Madras (1922) especially intended for the benefit of cottage industries. The elaborate accounts and returns required under the Madras Act

* India in 1926-27, p. 331.

have been found by experience to detract from its usefulness and suitable amendment is said to be contemplated. Before concluding we may observe that apart from encouraging deserving handicrafts that already exist, something may also be done to start new industries which are likely to thrive as cottage industries.

CHAPTER IV

INDUSTRIAL LABOUR.

§ 1. Growing Urgency of Labour Problems in India :—With the steady progress of large-scale industry and the rise of factory towns like Bombay, Calcutta, Cawnpore, Madras, Ahmedabad, Nagpore, Jamshedpur, etc., modern labour problems as understood in the West are slowly but surely coming into prominence in India. The slowness of the industrialisation of the country has, however, prevented any rapid growth of a landless proletariat class in factory towns solely dependent upon industrial employment as in England, where the Industrial Revolution was responsible for the creation of a large class of factory workmen permanently divorced from land. Though our labour problems are not, therefore, as formidable as in the West today, the time is not far distant when they will assume similar dimensions. The War has created a new mass awakening and the workmen are becoming more and more conscious of their importance, privileges and rights. The War-time and post-War rise in prices which has greatly increased the cost of living has led to labour unrest and is forcing labour to organise itself so as to safeguard its interests. The Indian labour movement has now been definitely linked up with the international labour movement, and India's labour representatives now attend the International Labour Conference held annually. India has been already recognised as one of the first eight countries of industrial importance after an examination of her claims by experts appointed by the League of Nations.* Lastly, the national importance of ensuring an adequate supply of an efficient and contented labour force in building up an up-to-date industrial civilisation in India is being understood more and more by Government and the people.

* These claims were based upon the number of workers, industrial, agricultural, and maritime; mineral production; railway mileage and traffic statistics, industrial horse power; export of manufactured goods; and statistics of industries. See the Memorandum of the India Office submitted to the League of Nations, Labour Gazette, Bombay 1922, pp. 29-35

§ 2. Growth of Factory Labour:—No systematic records of labourers in all classes of factories were maintained before 1892. During the period 1879–1880, 47,855 persons were found in the Cotton Mills of the country, while the Jute Mills accounted for 59,222 workmen in 1889. * Between 1892 and 1926, the number of factories subject to the Indian Factories Act rose from 650 to 7,251 and the average daily number of operatives employed in them increased from less than one third of a million to 1,518,391 during the same period. † Although, comparatively small numbers have migrated into the towns, “the constant interchange that is taking place between the towns and villages affects the lives of many who have never visited the towns themselves. ¶ With the further industrialisation of the country it is obvious that the number of factory workmen will increase.

§ 3. The total strength of Indian Labour:—Though industrial labour engaged in factories is only a small fraction of the population, the Memorandum submitted by the India Office to the League of Nations gives the following striking figures regarding the total strength of her labour supply :—

Agricultural Workers (excluding peasant proprietors) who come within the scope of the work of the International Labour Office	77,664,886
	27,810,130
Maritime workers, lascars etc.	141,000
Workers in industries, including cottage industries, mines and transport	20,219,000

If the test of total workers alone were applied India is easily the first country in the world. India with 100,00,000 occupied males more than in the whole of Europe completely overshadows the four countries which are immediately concerned, the figures for which are as follows:—

Italy	11,275,000	Belgium	2,600,000
Japan	18,800,000	Switzerland	1,777,000

* See R. K. Das: *Factory Labour in India*, pp 15–16.

† See India in 1926–27, p 112,

¶ Broughton: *Labour in Indian Industries*, p 1

§ 4. Supply of industrial labour and its migratory character:—

As noted above the factory labourers in India do not constitute a wage-earning class exactly corresponding to the factory labourers in western countries. In these countries there is a permanent class of industrial workers completely divorced from the land and solely dependent upon their wages. In India, on the other hand, though there has latterly been a tendency for the rise of a permanent class of factory workers in industrial centres like Ahmedabad and Cawnpore, most of our factory labour is migratory in character. The average Indian factory operative is agriculturist first and agriculturist last. He is a factory hand by necessity and usually never severs his connection with his village and his small holding. In many cases he goes to the towns alone, leaving his wife and children behind him in the village where he has got his home and takes the first opportunity of returning to it. The causes of this periodical migration of labour from the villages to the towns may be briefly examined. We have already referred to the growing class of landless rural labourers who are the first to feel the pinch of agricultural distress. The improved means of communication enable them to leave the villages in search of work and higher wages in the factories, workshops, dockyards, mines, plantations and the great public works like railways and irrigation. Many of the petty holders of land are also compelled to seek temporary employment in the towns. The progressive ruralisation of the country, the increase in the total population and the general land hunger have intensified the pressure on land and led to the creation of small holdings which are unable to support their owners, especially in dry tracts like the up-country districts of the Bombay Deccan. In some provinces like the United Provinces, Bihar and Orissa and certain districts like Ratnagiri in the Bombay Presidency, the density of the population and the pressure on land are so great that the petty landholders are under the necessity of migrating every year to the towns during the slack agricultural season. The Joint Family System facilitates such migration as some members of the family can leave the village without having to break up their home or giving up their land as these can be left in the

charge of other members who remain behind. Sometimes the agriculturist may seek employment in the towns to evade the village money-lender or to earn enough for buying cattle or more land. Sometimes the village menials and drudges belonging to the depressed classes migrate to towns in the hope of bettering their prospects. Most of these workers, as said above, maintain their connection with the village and return in large numbers to their fields on the advent of the rains. Thus the bulk of the labour supply in industrial centres like Bombay and Calcutta and also in mining areas is of a floating character.

§ 5. The effects of the Migratory character of Industrial Labour:—This feature of our industrial labour leads to some important consequences from the point of view of the methods and habits of work and consequently the efficiency of the workman. In the first place, as the labourer is always looking forward to the time when he would be able to go back to his village, he cannot rein himself down to steady whole-hearted work in the factory and this prevents his acquiring a high standard of technical efficiency. Not being dependent solely upon work in the towns and treating factory work as a disagreeable necessity, he is prevented from developing a sense of responsibility as an industrial worker with the consequence that dismissal and unemployment in the towns lose more than half their terrors. Again, increase in wages does not seem to evoke a response by way of more efficient and steady work, but often results in increased absenteeism. Another consequence of the migratory tendencies of Indian labour is that the employers have to engage a larger number of hands than are strictly necessary so that a sufficient number should remain available even though some may return to their villages. This either places an undue burden on industry or leads to low wages. The incessant migration of the Indian workman increases the difficulties of his reinstatement in the towns and leaves him at the mercy of the money-lender, the jobber or the labour supplier, the foreman and the liquor-seller.* It is true that the frequent visits to the village enable the operative to recoup his health in the more conge-

* See B. Hurst : *Labour and Housing in Bombay*, Foreward by Sir Stanley Reed, pp. vi and vii.

nial and healthy surroundings on the country side, but it is also true that he often returns a physical wreck from the town and is the means of spreading certain diseases in the villages. It goes without saying that this migratory character of a large body of workmen subjects the town industries to serious inconvenience and uncertainty.

§ 6. The sources of Labour Supply at some important industrial centres:—We may illustrate the migratory character of industrial labour by analysing the supply of labour on which some of the more important industrial centres depend.

(1) *Bombay*:—The principal industry of Bombay is the Cotton Mill industry. Other industries are connected with railway workshops and engineering shops, dock-yards, oil and flour mills, tanneries, iron and brass foundries, chemical factories, electric works, printing presses etc. Bombay is very largely dependent on imported labour. 84 per cent of the inhabitants of Bombay were returned by the Census of 1921, as having been born outside the city. The Deccan and the Konkan, especially the Ratnagiri district, are the chief sources of Bombay's labour supply. Other sources are, Kathiawar and Cutch, and even distant provinces like the United Provinces, Madras and Punjab and the French and Portugese Settlements send out some of their men to Bombay.*

(2) *Ahmedabad and Sholapur*:—The other centres of the Cotton Mill industry in the Bombay Presidency have a more permanent and less heterogenous labour force than Bombay. In Ahmedabad 60 per cent of the population are born in the city itself, and 23 per cent are immigrants from other parts of India, the remainder being drawn from the Bombay States and Agencies. Sholapur presents an even more satisfactory position in this respect. Nearly 64 per cent of the total population are actually born there and only 27 per cent come from outside the province mostly from the neighbouring state of Hyderabad.†

(3) *Calcutta*:—Calcutta with its suburbs where the principal industries, such as the Jute Mills are concentrated, relies not only on imported labour like Bombay, but what is more, depends,

* B. Hurst : op. cit. Ch. II.

† Broughton : op. cit. p. 84.

much more than almost any other centre, on labour from other provinces, such as the United Provinces, Bihar and Orissa, Madras and the Central Provinces. The smaller and decreasing share taken by the Bengali in contributing to the labour supply has been attributed to the fertility of the land and the dislike of the Bengali for factory work.

(4) *Cawnpore* :—Cawnpore is another important industrial centre and is the principal industrial town of the United Provinces. While the textile industry is the chief industry there are also tanneries and leather factories, engineering works, oil, flour and rice mills, chemical works, sugar factories etc. Labour is comparatively plentiful and is freely drawn from the densely populated rural districts which surround Cawnpore. The existence of comparatively satisfactory housing conditions has led to a more settled factory population here than elsewhere. * (5) *Madras* :—The Industrial development of Madras has been hampered by its deficiency in coal. It has a few large cotton mills and tanneries and leather factories. Madras depends upon its own local supply of labour to a far greater extent than Bombay, and, in fact, the province as a whole sends out a large number of persons to Burma, Bombay, Bengal, Mysore, Ceylon etc. "No less than 95 per cent of the total inhabitants of Madras city were born in the province itself and of these two-thirds were born in Madras itself; and the bulk of the remaining population came from adjacent districts such as Chingleput and the North and South Arcot." Moreover, the proportion between the sexes is fairly equal, 52·5 per cent being males as against 66 per cent in Bombay. This explains the greater stability of the labour force in Madras as compared to Bombay. The number of industries competing for labour, being small, the worker is anxious to stick to the employment he may have got because the chances of his finding alternative employment are slighter than in Bombay.†

§ 6. Labour supply in Mining Centres :—Mining, especially Coal-Mining is an important organised industry in Bengal and

* Industrial Commission's Report, p 29

† Broughton : op. cit. p. 141.

the principal industry in Bihar and Orissa. The labour for the Bengal coal fields is obtained from the backward cultivating tribes of the Santals and Bauris living on the borders of Bihar and Orissa. In Bihar and Orissa, coal-mining is carried on mainly by local labour, though the United Provinces and Central Provinces also contribute to the labour supply. The supply of labour in the mining centres is insufficient and intermittent. Only a small proportion of the workers reside permanently at the mines. The rest are usually small cultivators or agricultural labourers who return to their villages for the sowing and harvesting operations.

§ 7. Scarcity of Industrial Labour:—We have already† referred to the alleged scarcity and dearness of labour, and we have argued that the scarcity is felt not because of a real deficiency of numbers but because of the various factors which prevent potential labourers from being drawn into industrial areas. The true explanation of the scarcity must be sought in the appalling housing conditions in towns like Bombay, the lack of correspondence between wages and cost of living, the absence of a suitable labour-recruiting organisation for overcoming the conservatism and ignorance of the villager and his natural reluctance to wrench himself from his fixtures, especially in view of the practical impossibility of his taking his family with him. All these causes have from time to time been reinforced by a sudden shrinkage in the supply of men prepared to brave the various discomforts of life in the cities, on account of the heavy mortality caused by famines and epidemics like plague and influenza. While conditions on the side of supply have remained more or less the same, there has recently been an appreciable increase in the demand for labour owing to an extension of industrial enterprise, especially during and since the War. The migratory character of the industrial labour and its low standard of efficiency further emphasise the feeling of labour scarcity. Skilled labour is particularly difficult to get and this is of course due to the very meagre facilities that exist for training labour for modern industry. The scarcity of men

† See Chap. III, pp, 87-88, Vol. I.

of the *maistry* or foreman class possessing the requisite technical and business experience has also been ascribed to "the average educated Indian's aversion to all forms of manual work."*

§ 8 Factory life in India:—Let us now proceed to consider the conditions of factory labour in industrial towns like Bombay. No greater contrast can be imagined than that between the conditions of life and labour in villages and those in the towns in India. The agriculturist labourer who is accustomed to out-door work in open air with his family and fellow village folk, finds himself under altogether different conditions in an industrial centre like Bombay, where he must work 'crawling coop'd' under the roof of a factory amidst the din and whirr of machinery and in the company of other workers most of whom are total strangers to him. He is, if possible, even more uncomfortable when he returns to his miserable dwelling in a hideous overcrowded *chawl* in which home life is generally out of the question. The workman is forced to leave his family behind owing to many difficulties, the most serious of which is that of securing accommodation even on the most modest scale for maintaining family life.† Sometimes he is lucky enough to secure a job at once through the good offices of a friend. Often, however, he has to wait, and even when he gets employment, it may be only as a *badli* (substitute) for a permanent hand who may be temporarily absent.

§ 9. Methods of recruitment:—In this connection a word may be said regarding the methods of recruitment. In Bombay, each jobber (foreman of a department) is expected to find workers for his department. The mill management does not directly recruit the required labour. Personal recruiting by contractors going round the countryside may be necessary in exceptional cases as in the Assam Tea gardens, but it is no longer generally so. Still the foreman or the overseer is usually the

* Dr. Pillai: *Economic Conditions in India*, p 241,

† Without making it in the least a matter for complaint, it may be stated that the Factory Laws, by putting various restrictions on the employment of women and children, also make it difficult for the labourer to bring his family along with him.

man through whom the labour is secured. He has influence with the people living in his *chawl* and induces them to accept employment in his mill. Sometimes his operations extend to the people of his village whom he attracts by painting much too rosy a picture of town life. The jobber manages to make himself indispensable to the workmen in a variety of ways. He lends them money, advises them in family affairs and arbitrates in disputes. Since all labour is recruited through him, the newcomer generally finds that the only way of getting employment, temporary or permanent, is to bribe him.* This system of recruitment obviously cannot secure the best and the most efficient labour. It leaves too much power in the hands of the jobber who recruits such men as pay him the largest commission or as he may be interested in. The direction of reform would be towards a stricter supervision by mill officers and direct recruitment by them.†

A similar system of recruitment of labour prevails in the Jute Mills of Calcutta. The mill-workers are recruited by and employed under a class of men known as *Sardars* (overseers), usually themselves of similar origin to the hands they supply. The millowners complained before the Industrial Commission that this system was an obstacle to progressive management and did not conduce to industrial peace, but they professed their inability to alter matters. Extensive bribery known as *dasturi* (unacknowledged commission) and petty exactions swell the monthly income of the *Sardar* to four or five times his wages. Even the pay-clerks 'are known to reap harvests of this kind. Women workers also share with men the burden imposed by the overseers, but are particularly liable to be oppressed, especially if they happen to be widows.'§ In the Bombay Cotton mills, it is usual to have women overseers known as the *Naikins* or forewomen in the departments where women work, such as the winding and reeling departments. They are as a class considered to be persons of low morals and often abuse their power over the young girls and women workers under them.¶

* See B. Hurst : op. cit. pp. 46-47.

† See Textile Tariff Board's Report, para 65.

§ Kelman : op. cit. pp. 108-9.

¶ B. Hurst ; op. cit. p. 53.

§ 10 The methods of payment of wages:—In most Bombay mills wages are paid once a month, usually on the 15th of the month next following the one for which wages are earned, so that a new recruit has to wait for six weeks before he can get his wages. This is a source of much hardship and accounts for a large part of the indebtedness of the factory population. In fact, indebtedness is as much a feature of town life as of village life. The millowner's justification for holding wages in arrears is that this is the only method of preventing his labour force from deserting him without notice. The system of monthly payments necessitates at least one month's notice from a workman desiring to leave. Many new workmen, ignorant of this, leave without notice and thus forfeit a month's pay. This practice of payment after long intervals prevails also at other industrial centres in India, though generally speaking it is not as rigorously enforced as in Bombay. In the Calcutta Jute mills, weekly wages are paid and only a week's wages are held back. In Ahmedabad, wages are paid by the *hapta* or intervals of 14 to 16 days. The Calcutta plan appears to be preferable and ought to be introduced elsewhere. It might at first lead to increased absenteeism and unsteadiness of mill labour, but in the long run it will be found to work and to conduce to the greater convenience of both the parties.

The Government of India have already made a move in the matter of regulating by legislation the periods of wage payments. Local Governments were asked in 1924, September, to collect the required information which revealed a very unsatisfactory state of affairs. In 1926, the Government of India prepared a draft scheme which provided for the setting up of statutory limits within which wages must be paid. They opposed, however, the consideration in the Assembly of Dewan Chamanlal's Weekly Payments Bill, owing to the generally adverse opinions of the Provincial Governments and an apprehension that public opinion would not support such a bill and that the bill, even if passed, would remain a dead letter. They declared, however, their willingness to introduce suitable legislation to check or eliminate the abuses connected with the existing methods of payments. ‡

‡ The Indian Year Book, 1928, p. 506.

§ 11. System of fines :—Deductions of fines from wages for bad workmanship, or loss of materials, or depreciation and damage of machinery are common, and millowners in India claim wide discretion in imposing such fines for ensuring a certain minimum standard of work and for enforcing discipline. It is alleged that much loss accrues to the employers though the irregular attendance and general indifference of the workers, the constant replacement of labourers by substitutes etc. There is a general feeling, however, that the system of inflicting fines is much abused in India, and that the evil has reached such proportions as to require special steps being taken to cope with it. The experience of Western countries suggests that legislation is necessary to keep the fines within reasonable limits and prevent their arbitrary use. It is also suggested that the fines, so far as they are permissible, should be spent upon welfare work for the benefit of the operatives as a body. The Government of India have asked (in June 1926) the Local Governments to supply them with the necessary information so as to enable them to introduce suitable legislation for the regulation of deductions from wages on account of fines.*

§ 12. Hours of work for men:—We shall discuss the statutory regulation of the hours of work in the section dealing with Labour Legislation. Here we shall confine ourselves to the existing hours of work at the principal industrial centres. The Factory Law of 1911 limited the hours of work to twelve per day for adult males in the textile factories. The Bombay millowners, however, pleaded that the real hours worked were about eight owing to want of continuous and rigid application to duty. In fact one of the grievances of the employers of labour in India has always been that the Indian mill-hand is incapable of steady and continuous work. He is given to loitering and loafing away his time under various pretexts. Men are often found to be absent from their machines and spare hands have to be employed to attend to the machines of the idlers. The Indian Factory Commission (1908) declared that, "while the Indian Factory worker may work hard for a comparatively short period, his natural inclination is to spread

* Indian Year Book, 1928, p. 506

the work he has to do over a long period of time, working in a leisurely manner throughout and taking intervals of rest whenever he feels disinclined for further exertion." This habit of loitering has been attributed to various causes. The excessively long hours of work—12 to 14 hours—which prevailed, especially before the passing of the Factory Acts of 1911 and 1922, are held to be the chief cause. Dr. T. M. Nair in his Minute of Dissent to the Report of the Factory Commission calls it "a manifestation of the adaptive capacity, which all human beings possess more or less, a device to reduce the intensity of labour as a safeguard to his physical well-being", and emphatically protests against the charge that the Indian labourer has ingrained habits of idleness. Climatic conditions, feeble physique and the agricultural interests of the labourer are also suggested as other causes.* With the reduction in the hours of work and improved sanitary conditions, and ventilation in factories and better supervision through the institution of the pass system, the loitering habit will be largely checked. There is, for example, less loitering in the Calcutta Jute mills, where workers work in shifts for shorter hours, and in the Engineering shops, where also the working day does not exceed eight hours.

Even before the Factory Law of 1922 which restricted the hours of work in all factories to 11 per day and 60 per week, the Bombay mill-hands had been able to compel the millowners, as the result of a great strike, to reduce the hours to 10 per day, so that the legal limit exceeds the hours now generally worked in Bombay. Work starts usually at 7 A. M. and lasts till 6 P. M. with an hour's interval from 12 to 1. The system of double shifts has been abandoned owing to slack trade and scarcity of labour except in a few mills where there is a double shift of 8 hours for adult workers. Before the Factory Act of 1922 the men in the Jute Mills at Calcutta worked principally in one shift of 11½ hours a day with an interval of an hour and a half. The Factory Act of 1922, while it has not affected the hours of work in the Bombay textile mills, has conferred a general benefit on all factory workmen in India. Turning to the average hours of work for adult males in the factories in Bri-

* See Pillai : op. cit. p. 237 and B. Hurst : op. cit., p. 61.

tish India in 1926, in 26.8 per cent of the factories the normal weekly hours of work were not more than 48; in 12.72 per cent not more than 54 and in 60.48 per cent, they were above 54.

§ 13. The hours of Work for Women:—Under the Factory Act of 1922 the hours of work for women are the same as in the case of men, viz., 11 per day and 60 per week. Actually for Bombay City and Island about 91 per cent of the men and 32 per cent of the women are on a ten-hour day and the remainder work for less than 10 hours.* The average weekly hours of work for women in all factories in British India in 1926 were less than 48 in 31.22 per cent of the factories, above 48 and not above 54 in 12.75 per cent and above 54 in 56.03 per cent. In Bombay, nearly 75 per cent of the factories employing women have hours of work of over 54 per week. The hours of work are usually from 7 A. M. or 8 A. M. to 5 or 6 P. M. with an hour's interval at midday as in the case of men. In the Calcutta Jute Mills before the Act of 1922, there were three shifts for the women, two of 9½ hours a day and the third for 9 hours. Some changes have been made to bring the shift system into conformity with the Act of 1922.

§ 14 Hours of work of Children or half-timers†:—In the Bombay Cotton Mills, the hours of work for children were reduced to 5 after the strike of 1920 and are thus below the standard of 6 hours laid down by the Act of 1922. They work in two shifts from 7 A. M. to 12 noon and 1 P. M. to 6 P. M. In Calcutta before the Act of 1922 there were six shifts for children and they all worked six hours with varying rest intervals. Turning to the average hours of work in British India, the percentage of factories in which the weekly hours of work for children were more than 30 was 70.08. In Bombay, out of the 222 factories for which information was available, in 47.75 per cent of the cases, the hours of work were below 30 per week, and in 52.25 per cent, above 30 per week. It is noteworthy that only in the case

* *Wages and Hours of Labour in the Cotton Mill Industry*, (Bombay Labour Office), 1923, p. 18.

† For the age-limits of children see below, under Labour Legislation.

of children are the hours of work lower in the Bombay Presidency.*

§ 15 The evil effects of the employment of women and children:— The employment of women and children in factories gives rise to some of the most serious evils of modern industrialism and leads to special hardships in the circumstances of India, † The life of a married woman engaged in a factory is very hard as she is wage-earner as well as domestic drudge of the family and the excessive pressure of work leads to serious nerve and tissue waste. ¶ The children are mostly left to themselves as very few factories provide creches. Before the Factory Act of 1922, children were even allowed inside the factory with all the attendant risks of accident and injury to health. The absence of maternity benefits and the usual over-exertion to which she is subjected right up to confinement and which begins again almost immediately after, work further havoc with the health of the female labourer. The absence of suitable medical facilities is another great hardship.

The employment of children is even more liable to abuse. Before the Factory Act of 1922 children certified to be 9 years of age were allowed to be employed 7 hours daily. In practice, this age-limit was much lower owing to the difficulty of ascertaining the age correctly and the abuses of the Age Certificate system. The law was also

* See Annual Statistics relating to Factories in India, 1926.

† We have referred more than once to the housing difficulties in industrial towns like Bombay which compel many men to go and live single in towns. This accounts for the small percentage of women and children employed in Indian factories. In 1926, the total number (1,518,391) of persons in factories was distributed as follows:—1,208,623 (80 per cent) men; 249,669 (16 per cent) women and 60,014 (4 per cent) children. The percentage of female labour is 21 in Bombay and Madras, only 13 in Bengal, and in Burma it is as low as 9. As regards child workers in the Bombay Presidency, only 6.85 of the operatives, are children. The inability of the labourers to take their family along with them puts many women and children beyond the reach of the evils of industrialism but, on the other hand, it is disastrous to the physical and moral health of the male workers.

See Labour Gazette, Bombay Feb. 1923

¶ Final Report of the Lady Doctor on Maternity Benefits, Bombay 1922.

evaded in some cases by the children working in two mills. The Factory Inspectors found it an impossible task to control these abuses. Hence the Factory Law of 1922 raised the age-limits of half-timers to 12 and 15 respectively, and reduced the hours of work to 6, in the hope that the results of the possible evasion of law through false declarations of age would be less serious than under the old system. Another important reform introduced in Bombay was the appointment of whole time surgeons. All this has led to a welcome decline in the number of children employed in factories.* It is perhaps necessary to add that the enhanced age-limits must be utilised for giving a suitable education to the children. Proper education imparted before the children are employed in factories is much better than education given in indifferent schools maintained by a few mill-owners for half-timers, even if the further objection that the combined strain of factory work and schooling may be too much for such young persons to bear is waived.

§ 16. Trying conditions of work in the mills :—In the interests of the health and efficiency of the operatives special attention is necessary to such matters as ventilation, the regulation of humidification in factories, arrangements for meals, bathing and latrine accommodation etc. Conditions in all these respects are gradually getting better, but there is still ample scope for improvement. The problem of ventilation is one of light and free air in motion and presents special difficulties in cotton mills, which in large cities like Bombay are built in blocks of several storeys, where roof light is not possible except on the top floor. "Proof of the difference of efficiency in work done in well and ill-ventilated mills in India has already been secured on a small scale. Experiments that have been made show a fall in efficiency during the hot weather in an ill-ventilated weaving shed as reaching twenty per cent, while that in a well-ventilated shed was less than seven per cent."† Humidification presents another difficult problem. India does not possess the advantage of a naturally humid climate which is required for spinning and

* See Report on the Wages and Hours of Labour (1923), Bombay, p. 3.

† Kelman : op. cit. p.198.

weaving of cotton. To avoid breakage of thread and loss of material in the tropical climate of India, artificial humidification of factories is necessary. Such humidification, especially when effected by the letting in of steam and use of impure water, is injurious to the health of the operatives. The Government of India have taken a step in the right direction by the appointment of an expert advisor on humidification to ensure the adoption of the best possible methods of humidification. In most mills and factories in India, there are no proper arrangements for the meals of the operatives. The meal is hurriedly prepared in the morning and carried to the factory either by the workman or brought to him later by a messenger. It is eaten in the open factory yard weather permitting, or else inside the machine sheds. A very small number of mills, such as the Buckingham and Carnatic Mills, Madras, have supplied dining sheds for the different caste people employed by them. There is an urgent need for suitable canteens which can be patronised by workers of both sexes. This will also lessen the strain on the woman worker and make the midday recess a real time of rest for her. Supply of pure drinking water, arrangements for bathing, so essential in a tropical country like India, and sanitary latrine accommodation are further points in regard to the conditions in factories to which the employers of labour have not yet learnt to attach sufficient importance as increasing the comfort of the worker and improving his efficiency.

§ 17. Absenteeism in Indian factories :—One of the embarrassing characteristics of factory labour in India is its intermittent character. The large percentage of absenteeism among the operatives makes smooth working of the factory extraordinarily difficult. "It is well known that in the cotton mill industry (as perhaps in other industries) the worker is frequently absent either through sickness or voluntarily because he has earned sufficient to keep body and soul together and lacks the will to increase his wages to the maximum that could be earned."* The millowners assert that there is an increase in absenteeism after increase of wages or payment of wages and bonus.

* Wages and Hours of Labour in the Cotton Mill Industry, (1923). Bombay, page 7.

The percentage of absenteeism (which in the case of Bombay varies on an average from 11 to 13 per cent) shows seasonal variations reaching its maximum in the monsoon months (when it may exceed even 25 per cent) and the festival and marriage seasons, being thus highest from March to June and lowest in December and January.* In Calcutta there is a large annual exodus in the hot season because the jute industry season is slack after winter and because the climate in the early part of summer is particularly trying. As we have already seen, Ahmedabad's smaller percentage of absenteeism is due to the fact that its mill operatives are mostly drawn from an industrial population which has been settled in the city for generations.

Absenteeism on this scale necessitates the maintenance of an excessively large muster roll and leads to the employment of inferior substitutes casually recruited, thus seriously detracting from the efficiency of labour. It is, however, not easy to suggest remedies. Attendance allowances have been tried. One of the Bombay mills has successfully attempted the plan of imposing some penalty by way of refusing employment for a few days in cases where there are no legitimate grounds for the absence. The Textile Tariff Board suggest the formation of labour reserves which would make a casual *badliwala* unnecessary and also facilitate the grant of leave. †

The rapid turn-over of labour in factories is another drawback of industrial labour in India., and is closely connected with absenteeism. It is alleged by the Factory Labour Commission that "The Indian operative is fond of changes, he prefers to wander from mill to mill rather than to remain settled, and the slightest causes are apparently sufficient to determine him to leave one employer for another," though the inducements to change are occasionally pecuniary.¶ This results in a rapid turn-

* B. Hurst, op. cit, p 59

† Textile Tariff Board's Report, para 60.

¶ Mr. R. K. Das, however, is of opinion that the factory workers are not floating nor desultory in habit, nor are they fond of changes to any greater extent than in other countries. There are factory employees who have remained in the same mill for 20 to 30 years. Dissatisfaction with

over of labour-force, and the personnel of the workers in mills in industrial centres like Bombay, Madras and Nagpore changes almost completely in about a year and a half on an average. Such a rapid turn-over causes a needless increase in the costs of production and is highly detrimental to the efficiency of workers.

§ 18 Efficiency of Industrial Labour:-The position as regards the alleged inefficiency of Indian labour needs to be clearly stated. Indian labour is generally regarded as much less efficient than European labour. If by this we mean that the European labourer is capable of turning out much more work than the Indian labourer in a given time, it will not be possible to contradict such a statement. Several attempts have been made to prove this mathematically by a number of elaborate calculations. In his evidence before the Industrial Commission, Sir Alexander McRobert stated that the English worker was 3.5 or even 4 times as efficient as the Indian. Sir Clement Simpson calculated that 2.67 hands in an Indian cotton-spinning and weaving mill are equal to one hand in a Lancashire mill. Dr. Gilbert Slater, however, points out that in this calculation the inferiority of the Indian worker is overstated.* The difference in the number of weavers employed to attend one loom in India and England does not by itself provide an accurate measure of the difference in efficiency of Indian and English labour. In India, a larger number of workmen are employed because the value of the additional output is greater than the increase in the wage bill. In England, wages being much higher, economy in the number of workmen employed is imperative. Dr. Slater, however, admits that though the inferiority of Indian labour is generally exaggerated, it is real enough, and indeed, it need cause us no surprise if we remember the much superior physique, the greater intelligence, amenability to discipline and capacity for steady continuous toil of the English labourer. But although there can be no doubt about the greater effectiveness as a worker of the English labourer, it is necessary

hours of wages leads them to change one mill for another and the absence of standardisation of wages intensifies the motive to change. R. K. Das : *Factory Labour in India*, pp. 44-45.

* See Pillai, *op. cit.*, pp. 208-209.

to accept with caution pseudo-mathematical statements such as those alluded to above. The problem of the relative efficiency of English and Indian labour, cannot be solved by the method of difference because of the entirely different conditions of work. The smaller outturn in an Indian mill cannot be wholly put down to the inferiority of the Indian operative. For, his lower productivity may partly be the result of relatively inefficient management. Moreover, as the textile workers in Bombay pointed out in 1889 in their petition to the Governor-General asking for the redress of certain grievances, he is handicapped by the badness of the raw material used in Indian mills. Owing to the inferior quality of the cotton, there is continuous breakage in thread and more men have thus to be employed. It is also complained that, unlike the Lancashire millowners, the millowners in India do not use the most up-to-date labour-saving devices and machinery.* One reason for this is that all machinery has to be imported from abroad, which makes it much more expensive than in England; and as wages are lower in India, this often determines the balance in favour of employing more hands rather than invest in the most up-to-date machinery and the latest labour-saving appliances. The employers cannot indeed be blamed for this, but it certainly renders the comparison between English and Indian labour unfair to the latter.

Granting, however, that the Indian labourer would almost certainly be found to be inferior, in the sense that his output would be smaller, even if other things such as the nature of machinery employed etc. were the same, the next question to be answered is whether Indian labour is also inefficient in another sense which turns on the relation between the work turned out and the wages paid. The Industrial Commission thought that Indian labour does not produce as cheaply as Western labour

* However, according to the report of the Lancashire representatives on the International Textile Factory Workers' Association delegated to India, mills in India as a whole compare favourably with Lancashire as regards construction of buildings, modern machinery and up-to-date labour-saving devices, but the workers are lacking in the skill, stability and stamina of their prototypes in Lancashire.

inspite of its lower wages. It may be pointed out in this connection that Dr. Nair argued in 1908 that "if one Lancashire operative is equal to 2.67 Madras operatives, then since the average monthly wage of a Lancashire operative is about Rs. 60 (£4), while that of a Madras operative is only Rs. 15 (£1), it is clear that for the same money the Indian millowner gets nearly double the work that an English millowner does." * This, however, amounts to saying that Indian labour is actually more efficient than English labour (taking efficiency in the second sense of the term), which is almost certainly untrue; and friends of Indian labour should note that it proves too much from their point of view, for if Indian labour is already twice as efficient as English labour (which, perhaps with the exception of American labour is generally regarded as the most efficient in the world), why trouble about making it still more efficient, say, by means of higher wages and the consequent improvement in the standard of living? The case for better wages is clearly much weakened by such tactless defence of Indian labour. But apart from any tactical considerations, we think that, broadly speaking, at the present time, the principle of the economy of high wages will be found to apply to Indian labour, so that increased wages are likely to result in a more than proportionate increase of efficiency and that, however we conceive the matter, the present position is that Western labour is incomparably more efficient than Indian labour.

§ 19 Causes of the inefficiency of Indian labour:—As regards the causes of the inefficiency, their name is legion. But without attempting anything like a complete enumeration we may mention the principal ones. Some of the causes of the relative inferiority of Indian labour are permanent and others are temporary or remediable. To the former class belong the climatic conditions in India which are generally adverse to high labour efficiency. Thinking of the cotton industry we may note that Lancashire possesses a great advantage in its cold and invigorating climate denied to most parts of India where the industry is located. Again, the artificial humidification which is necessary in India is at best a poor substitute for the

* Pillai, op. cit, p. 244.

naturally moist climate of Lancashire and can inflict serious injury on the health of the operatives unless it is properly regulated. The causes susceptible of remedy, such as the very unsatisfactory conditions in Indian mills as regards ventilation and sanitation etc., have already been referred to. Further, it may be urged that the hours of work, although shortened recently by legislation, are still much too long, especially for a tropical country like India and there is probably much truth in the suggestion that the slackness and listlessness of the Indian worker is a kind of protective device which he unconsciously adopts to prevent constitutional break-down which strenuous labour for the long hours of work would otherwise inevitably bring about.

It is undoubtedly a fact that the physique of the average Indian worker is inferior to that of an average English worker. This is due especially to two causes, (a) the ravages of disease and (b) a poor dietary. While, as we have seen, the rural areas are by no means free from the ravages of major diseases like malaria, plague, cholera, influenza, Kala-Azar, hook-worm etc., their incidence is especially heavy in congested industrial areas. The awful slums where the labourers have to reside are first-rate breeders of pestilence and provide most ideal conditions for its rapid spread. An organisation for the improvement of public health, which would include the supply of pure water, unadulterated food, and a proper drainage system, is absolutely necessary along with better medical facilities and a system of insurance against sickness of industrial workers. We shall presently say something of the attempts in this direction that are being made in Bombay and other industrial centres.

As regards the effects of a poor dietary this is a question which concerns the whole Indian population and will be discussed elsewhere.

§ 20. Conditions of Housing:--The unbelievable overcrowding and appalling conditions of sanitation such as exist in Bombay have much to answer for in respect of the instability of labour in the towns and its low efficiency. These evils are to be seen perhaps in their most staggering form in Bombay and are not equalled in any other

industrial centre, not only in India but anywhere else in the whole world. In some of the industrial areas in India where factories have been established at some distance from the towns, the problem of housing and sanitation is comparatively simpler. The labourers are often housed in the neighbouring villages or in dwellings that take the form of single-story lines erected by the employer who can acquire the necessary land without much difficulty. The second stage of development and congestion is typified by such cities as Madras, Cawnpore, Nagpore, Ahmedabad and in a very large proportion of industrial areas round Calcutta. Here land is far cheaper than in Bombay and Calcutta, and accommodation usually consists of single-storey huts in groups known as *bustees*, erected by persons other than the owners of mills and rented by mill-hands on fairly reasonable terms. Housing conditions here are no longer as easy as in the villages and require close supervision either by the millowners or by the local authority. In some cases, as at Cawnpore, Calcutta and Ahmedabad, the more enlightened factory owners have found it advisable to supply housing accommodation to the employees in the hope of commanding "the pick of the labour market, especially in the case of such fluid labour force as that on which the textile factories rely."* Conditions in Ahmedabad are particularly favourable inasmuch as land is cheap relatively to its cost in the cities, and the mills have usually provided themselves with large compounds. Moreover, the mills, unlike those in Bombay, are at fairly long distances from one another and this prevents workmen accommodated in buildings belonging to one mill from working in another mill.

The worst example of congestion is to be seen in Bombay to which the town of Calcutta proper comes a close second. Here conditions are altogether different. The haphazard way in which the city was allowed to grow up and the industrial areas were permitted to develop in the very heart of the city has led to the existing congestion and the difficulties in the way of betterment are unique in India. The rapid rise of Bombay in industrial importance is illustrated by the phenomenal increase in its population within a comparatively short period of time. At the time of

* Industrial Commission's Report. para 238.

the Census of 1872, the population was 644,405 and at the time of the Census of 1921, it had increased to 11,75,914 thus showing an increase of nearly 100 per cent between 1872 and 1921.

Though the extent of overcrowding and the proportion of bad to good *chawls* is often exaggerated there is no doubt that the actual state of affairs is shocking enough. "The majority of the working classes are housed in *chawls* or tenements which consist usually of single rooms, sometimes of double rooms or *gallas*, but never of more than two rooms. These *chawls* have for their object the housing—one is almost tempted to use the expression "Warehousing"—of large numbers of the labouring classes in as cheap a manner as possible."†

The vast majority (97 per cent) of the working class families live in single rooms, though the percentage for the whole population in the city is much smaller, viz., 66 per cent. The average number of persons per room in the case of working class quarters is 4.03. These figures stand in striking contrast with those in London where only 6 per cent of the total population live in one-room tenements with an average of 1.92 persons per room. While the worker lives in one room in Bombay, in France and Belgium he has two rooms, in Germany three, and in England and Wales even four or five. It must also be remembered that the practice of subletting is common among industrial

† B. Hurst, op. cit, p 20.

"The worst type of *chawl* consists of a two, three, or four-storeyed building, with single-room units either placed back to back or separated by a narrow gulley two or three feet wide, usually traversed by an open drain. The rooms, especially those on the ground floor, are often pitch dark and possess very little in the way of windows; and even the small openings which exist are closed by the inhabitants in their desire to secure privacy and to avoid the imaginary evils of ventilation. The ground floors are usually damp owing to an insufficient plinth; the court-yards between the buildings are most undesirably narrow and, therefore, receive insufficient sun and air. They are also very dirty. Water arrangements are insufficient and latrine accommodation is bad, though the latter is being steadily improved. A most insanitary smell hangs round these buildings". Industrial Commission's Report, para 241.

workers in Bombay which of course causes further overcrowding.* This practice is facilitated by the long hours of work spent outside the rooms and the sleeping in the open in fair weather.†

§ 21. The adverse effects of bad housing and sanitation:—
 “ Good houses mean the possibility of home life, happiness and health; bad houses spell squalour, drink, disease, immorality, and crime, and in the end demand hospitals, prisons and asylums in which we seek to hide away the human derelicts of society that are largely the results of society’s own neglect.”¶ Insufficient and bad housing is also one of the factors responsible for industrial unrest. All these evils are present to a smaller or greater degree in Bombay. One of the gravest and most striking evils is the heavy infant mortality in the Bombay slum areas. The rate of mortality varies inversely with the number of rooms in the dwelling-place. The highest rate reached in the worst localities is 828.5 per 1,000 registered births as against the average rate of 666.7 for Bombay in 1921. The heavy infant mortality, which we have already discussed,§ is due to a great variety of causes such as early marriage, maternal ignorance, lack of medical care and nursing,|| habit of drugging the child with opium, the growing difficulty of securing a sufficient supply of good milk, prevalence of venereal disease and the general poverty.

* According to the 1921 Census, 3,125 single room tenements contained two families and more. Of these 1,955 contained two families, 658 three, 242 four, 136 five, 42 six, 34 seven and 58 eight families and more. *Working Class Budgets Bombay*, Labour Office, pp 23-24.

† The predominant rents for single rooms are between Rs. 3-8 and Rs. 5-8 and for double rooms Rs. 7 to 10 for the working classes. The rents charged by the Improvement Trust, the Port Trust and the Municipality for the *Chawls* built by them are lower than the rents of privately owned *chawls*.

¶ Quoted from *The Great Opportunity*, in the *Working Class Budgets*, Bombay, p. 25.

§ See Chapter III, section 2, Vol. I above.

|| The employment of a limited number of municipal nurses and midwives whose duty it is to visit the homes of the poor and instruct and advise mothers, the establishment of maternity homes and milk-depots attached to them, and of infant welfare centres, the anti-prostitution campaign, together with the steps taken for improving housing and sanitation are some of the measures that have been adopted to tackle the evil of high infant mortality.

There is no doubt, however, about the direct causal connection between overcrowding and high infant mortality. Lastly, the appalling conditions of *Chawl* life and the absence of privacy have also a deterrent effect on those who wish to bring their families with them to the towns and have thus, in general, a very unsettling effect on the stability and efficiency of labour.

§21 Attempts at improved Housing:—Attention has already been drawn to the necessity of improved housing. While water supply, sanitation and drainage were improved, no heed was given for a long time to the removal of congestion and the destruction of the slums. Every year made the position more and more complex. The heavy mortality and the great exodus from Bombay that followed in the wake of the great plague of 1896 and the consequent paralysis of trade and industry brought matters to a head. And the Bombay Improvement Trust was established in 1898, “for the work of making new streets, opening out crowded localities, reclaiming lands from the sea to provide room for the expansion of the city and constructing sanitary dwellings for the poor and the police.”* The limited powers and funds of the Trust and want of proper co-operation between the Trust and the Corporation, together with its inevitable unpopularity on account of compulsory acquisition of property and demolition of buildings prevented rapid progress and led to the adoption of the policy of “slum-patching,” the development of a few building sites, the construction of a few *Chawls* and the development of main thoroughfares. In some cases the people dishoused did not avail themselves of the alternative accommodation provided and another congested zone was formed near the original demolished area, which thus rose in value and made it difficult for the Trust to acquire it. Still the Trust was able to do some highly useful work and provided 21,387 new tenements as against 24,428 tenements demolished. It constructed a number of much-needed broad thoroughfares, which serve incidentally the purpose of main air channels for the congested areas. The Municipality also had by 1920 provided 2,900 tenements for its staff and had sanctioned the construction of another 2,200. The Port Trust

* See B. Hurst : *Labour and Housing in Bombay*, p. 31.

has provided quarters for nearly 5,000 of its employees. In the meantime, the population of the city was increasing rapidly and the millowners did little in the matter of housing their operatives. In addition to the continuation of the scheme for the industrial housing undertaken by the Improvement Trust, the Industrial Commission urged other measures, such as the refusal of permission, with a few exceptions, to fresh industrial concerns to be established, the setting up of a special area for industrial development, the removal of the existing Railway Workshops at a reasonable distance from the city, supply of housing accommodation to their employees by Railways, Government Departments and public bodies, improved communications with the object of creating industrial suburbs, a definite standard of accommodation for industrial dwellings located in the city, and a programme of construction worked out and taken up by Local Authorities. It was under these circumstances that, at the end of the War, a bold and comprehensive scheme of establishing a Development Department for dealing with the problem was drawn up by the Bombay Government under the personal inspiration of Sir George Lloyd.* The funds were derived from the proceeds of a development loan of Rs. 9 crores and a 'town-duty' of one rupee per bale of cotton on all cotton entering Bombay.† The Development Directorate was formed in November, 1920, to co-ordinate the activities of the various bodies. A very ambitious programme contemplating the construction of 625 chawls, or 50,000 one-room tenements, between 1921-1929 was laid down at an estimated cost of Rs. 5.5 crores, providing accommodation for about 200,000 workmen, i. e., nearly one-sixth of the total population of the city. However, a large number of the tenements built (about 69 per cent) remain unoccupied. From an architectural point of view they are universally pronounced to be profoundly ugly structures and their inability to attract the workers has been attributed to difficulties of access, absence of bazaar facilities, cement construction, which makes the rooms warm in hot weather and cold in cold weather, and the

* See B. Hurst, *op. cit.*, pp 31-33.

† The duty is collected by the Municipality which retains 3/7ths of the proceeds for itself to enable it to supply funds for various improvement schemes.

high level of rents. The rents have recently been lowered and the Government have declared their willingness to lower them still further if whole *chawls* are taken up by large employers of labour, such as the Bombay Millowners' Association and Railway Companies.* So far, only the B. B. & C. I. Railway have availed themselves of the offer and rented 5 *chawls* at Worli for housing their employees. One *chawl* has been rented by the Bombay Municipality. The annual loss thus incurred (about 20 lakhs of Rupees) is met from the revenue from the cotton cess and other sources. Further construction of *chawls* (for industrial housing) has been held in abeyance until the tenements now provided are fully occupied. It is also believed that there has been a decrease in the labour population since the Census of 1921. The Bombay Development scheme was taken up in the post-War boom period when labour conditions were abnormal. The scheme which appeared so promising at first has proved a failure owing to an astonishing lack of imagination and forethought displayed in the manner in which the buildings were constructed. For example, no attempt seems to have been made to understand the actual needs of the expected inmates. Moreover, the high price of land during the post-War real estates boom in Bombay led to the adoption of the old bad *chawl* system, so that there was hardly any improvement either, as regards convenience or sanitation. Some attempts are, however, being made to correct these defects.

An interesting development scheme is being carried out at Ambernath, near Kalyan, which aims at creating a model industrial town, with all modern facilities with approach roads to all factories, staff bungalows and workmen's quarters, a shuttle service, market-place, water supply and sewage arrangements. In the town of Bombay proper, no new mills will be allowed hereafter. The Municipality, the Improvement Trust and the Port Trust are also carrying out their programme of development, and the Port Trust have constructed a new cotton depot at Sewri.

So far as the millowners are concerned, only a few mills, like the Jacob Sasson Mill, have provided housing accommodation

* See Textile Tariff Board's Report (1927), para 66.

to their operatives. The difficulty of procuring land on moderate terms in the vicinity of the factories, the absence of a guarantee that the operatives housed by a mill will not accept work in other mills, together with the reluctance of the operatives themselves to take advantage of such arrangements, have made slow progress inevitable. The operatives fear loss of liberty of action and probable ejection in case of strike and resent sanitary rules and discipline, the value of which they do not understand. Under these circumstances, the offer of the Improvement Trust to mill-owners to enable them to repay within fifty years the sums expended on chawls erected by the Trust has not been much availed of. More favourable conditions in these respects exist at Cawnpore, Nagpore, Ahmedabad and Madras, where the millowners have taken greater interest in the housing of their operatives with considerable advantage to both parties.

The Industrial Commission have recommended that Government should use its power to acquire land on behalf of the employers for the housing of labour subject to certain safeguards. Land may also be acquired at the cost of the Government or of the Local Authorities concerned, which they might lease at easy rates to employers for erecting industrial dwellings. They hold, however, that it would be undesirable and unjust to compel individual employers to house their own labour.

Thus it will be seen that the problem of industrial housing is receiving increasing attention in India at the hands of all the parties concerned, viz., Government, public bodies, and also, to some extent, employers of labour. The problem bristles with difficulties connected with finance, management, design etc., not the least of which arises from the total indifference of the workers themselves to the necessity of clean and sanitary housing. Proper education of the workmen regarding elementary hygiene and approximation of industrial dwellings to conditions obtaining in the villages, as far as possible, ought to go a long way towards ensuring clean and suitable dwellings and helping the stability of industrial labour.

§ 23. Low standard of living:—The low standard of living of the Indian labourer may be regarded as a further cause of ineffi-

ciency. It is both the cause and the effect of the low wages. The standard of living or the standard of comfort "deals with the distribution of the family income on necessities of existence, such as the requisite supply of cereals, of pure water, of clothing and of house-room; with conventional necessities such as tobacco and *pansupari* (betelnut), i.e., things which could be dispensed with but are so strictly demanded by the Bombay worker that he would give up the consumption of those articles which are really necessary for efficiency rather than go without these conventional necessities. There are, lastly, luxuries such as expenditure on amusements, and on festivals, which are really superfluous as a means towards production. There is waste when the worker consumes less than is strictly necessary for efficiency. It may be said that for each class of worker there is a more or less clearly defined income which is necessary for merely sustaining his family, while there is another income necessary for helping it on to full efficiency."* The standard of living of the Indian worker falls far short of what is required for full efficiency and is barely enough for sustaining his family. As the Enquiry into the Working Class Budgets, based on 2,473 family budgets in Bombay showed, the monthly income of the family (consisting of 4.2 persons: 1.1 men, 1.1 women and 2 children) is Rs. 52-4-6, the income of 75 per cent of the families ranging from Rs. 40 to Rs. 70 per mensem. There were 340 families with an income below Rs. 40 and only 39 families with an income Rs. 90 and over. With incomes of this order it is clearly impossible to maintain any satisfactory standard of living. The worker cannot afford sufficient wholesome food even supposing he utilises his income with the most complete wisdom. We have already described his sorry plight as regards shelter. His clothing is too scanty even for a warm climate. The expenditure on education is almost nil. The only furniture he can afford is limited to a few rough deal wood boxes, iron plate trunks, bamboo sticks, a country blanket, a worn-out mat, a few knick-knacks and cheap chromolithographs representing scenes from mythology.† A large part

* Working Class Budgets in Bombay, 1923, by G. Findlay Shirras, pp. 12-13.

† B. Hurst : *Labour and Housing in Bombay*, p. 63.

of his income goes to meet the interest on the debt he has almost invariably incurred. Besides the causes of indebtedness already pointed out earlier in the chapter, other causes are inordinate expenditure on marriages, funeral rights, festivals etc. Debt is rarely incurred for productive purposes.* The usual rate of interest charged is one anna per Rupee, or 75 per cent per annum, and compound interest is charged if the interest is not paid regularly. The interest on debt shows an average expenditure of nearly 3 per cent of the total monthly expenditure.

§ 24. Expenditure on drink:—The evil of drink is spreading in an alarming fashion among the factory labourers and, though no accurate figures are available, it is believed that at least 4 per cent of the total expenditure of the working classes, as shown by family budgets, goes on drink, the percentage being as high as ten in the case of the lowest class of workers like scavengers. The male worker—women rarely drink—frequently tries to relieve by drink “the hard and long day’s work in the mill under the scorching humid heat of an eastern sun.” (B. Hurst). As the Excise Commissioner, Bombay, observes, “It is clear that there is a very definite connection between the conditions of labour and consumption of alcohol. This may very probably be due in great measure to conditions under which the working classes live in Bombay”. There is some physiological connection between craving for drink and malnutrition due to poverty. The provoking part about the matter is that if the money spent on drink were to be used for buying more and better food, there would, of course, be less malnutrition. The worker is not only extremely poor but is also unable to manage his expenditure in the best possible manner and the expenditure on drink serves to aggravate his poverty which in its turn leads to an increase of drunkenness. Thus intemperance is a great bane to the working classes inasmuch as it impairs their efficiency, and as a result of the dissipation of their limited earnings which it involves

* According to the Working Class Budgets Enquiry in Bombay, 47 per cent of the families were in debt and the debt was the equivalent of two and half months’ earnings, (one month’s average earnings per family being Rs.52-4-6.).

renders them poorer consumers, than they might be. The increase in the tea-drinking habit, substitution of the cinema, the club and other forms of recreation for the tavern, and curtailment in the number of liquor shops along with rationing in mill areas are some of the remedies that are being tried to check the habit of drink.

§ 25. Wages:—It has been suggested above that increasing the wages of labour would be well worth while, since it is likely to be followed, at least up to a point, by more than proportionate increase of efficiency. This of course assumes that the increased wages are wisely spent. A better management of his earnings by the worker is a matter of education and conviction. At the same time an increase of wages is also necessary as a first step in order to key up labour to a higher state of efficiency. To say that labour is so inefficient that the present rate of wages more than represents its productivity and cannot, therefore, be raised, is to forget that higher wages will probably justify themselves by raising the productivity. It is argued that increase in wages is either dissipated in drink or leads to greater idleness on the part of the labourer instead of raising his standard of living and that consequently there is no improvement in his efficiency. It is, however, a libel against the hard-working labourer to suggest that, no matter how much he gets, he will either waste in a suicidal manner everything above what is needed for a bare subsistence, or by working less refuse to derive real benefit from the higher rate of wages. As sufficient answer, particularly to the former allegation, we may quote the following words of Prof. Pigou:—*

“ It is true that at any given moment the taste and temperament of persons who have long been poor are more or less adjusted to their environment and that a sudden and sharp rise of income is likely to be followed by a good deal of foolish expenditure, which involves little or no addition to economic welfare. If, however, the higher income is maintained for any length of time, this phase will pass whereas if the increase is gradual, the period of foolishness need not occur at all. In any case, to

* Pigou : *Economics of Welfare*, pp. 53-54.

contend that the folly of poor persons is so great that the rise of income among them would not promote economic welfare in any degree, is to press paradox beyond the point up to which discussion can reasonably be called upon to follow."

Another standard objection to raising the rate of wages is that the effect is likely to be very soon cancelled by an increase in population. This point has already been dealt with† and we have advanced the view that increase of wealth, although it may express itself partly in increase of numbers, may also be expected partly to result in raising the standard of living. *

The conditions of international competition are also alleged to be a formidable obstacle to the levelling up of wages. We have already referred to the difficulties of the Cotton Mill Industry, undoubtedly due in some measure to the severity of competition from Japan, which has not yet put into effect the Washington Conference Conventions. The fact that a country may gain a substantial advantage, at least temporarily, over another by sweating its workers and using them up "as omnibus companies use up their horses" cannot be denied. At the same time, it does not follow that other countries also must in self-defence adopt similar methods of sweating. Sweated trades eventually do not pay, as they are sure to result in diminished efficiency and, in any case, no civilised community can afford to ignore that equally important with the economic ideal of increase of production is the moral ideal of increase in the quality of human life. The proper method of equalising conditions of international competition is to get every nation to agree to secure certain minimum conditions of working, but even if a particular nation remains recalcitrant, protection against it must be sought in other ways than by imposing or acquiescing in a low standard of living for the workers tending permanently to keep down their efficiency.

§ 26. Wage Statistics : Nominal and Real Wages :—In connection with the rates of wages of industrial workers the follow-

† See pp. 91-92, Vol. I.

* According to Mr. Surve, M. L.C., Bombay, increased wages produce a higher standard of living in the village from which the Ratnagiri worker comes even before they appreciably affect his standard in Bombay.

ing statistics giving the main conclusions of the two enquiries by the Bombay Labour Office into the Wages and Hours of Labour in the Cotton Mill Industry in the Bombay Presidency may be of interest.

Average daily earnings (August, 1923).

Centre	Men			Women			Big lads & Children			All work people (a)		
	Rs.	as.	ps.	Rs.	as.	ps.	Rs.	as.	ps.	Rs.	as.	ps.
Bombay	1	7	2	0	12	5	0	12	3	1	4	2
Ahmedabad	1	6	2	0	12	9	0	11	4	1	3	10
Sholapur	1	0	0	0	6	4	0	9	1	0	12	9
Baroda State	1	0	6	0	10	10	0	8	0	0	15	3
Other Centres	1	0	1	0	8	2	0	8	8	0	14	0
Bombay Presidency	1	5	9	0	11	7	0	11	4	1	3	0

(a) Counting two half-timers as one full-timer.

These earnings are the actual earnings including monthly bonus and special allowances which are regarded as of the nature of wages, but excluding over-time pay, and annual bonus, if paid, and all remuneration in the form of grain or clothing or accommodation at rates below market prices or rentals.

The following figures give the average monthly earnings in Bombay City and in the Bombay Presidency.

Average Monthly earnings per head in 1914 and 1923

Centre		1914 May.	1923 August.
Bombay City.	Men	Rs. 18-6-8	Rs. 35-10-7
	Women	„ 10-0-10	„ 17-5-5
	Big lads & Children	„ 9-6-7	„ 17-14-0
	All workpeople	„ 16-6-3	„ 30-10-1
Bombay Presidency	Men	Rs. 17-0-8	Rs. 33-1-10
	Women	„ 9-0-1	„ 16-3-10
	Big lads & Children	„ 7-13-4	„ 16-9-6
	All workpeople	„ 14-11-11	„ 28-9-1

It should be noted, however, that the maximum or potential earnings of a worker for a full working month of 27 days, i. e., the earnings of a worker who is not absent on any working day in the month, are sensibly higher than those in the preceding table as will be seen from the following figures for August 1923.

Centre.	Men.	Women.	Big lads & Children	All work people.
	Rs. a. p.	Rs. a. p.	Rs. a. p.	Rs. a. p.
Bombay City. ...	39—1-6	20-15-3	20-10-9	34-0-6
Bombay Presidency.	36-11-3	19—8-9	19—2-0	32-1-0

The following figures, bring out the difference between real and nominal wages in the Cotton Mill Industry in the Bombay Presidency :—

Real and Nominal wages 100=1914

Bombay City.	Cost of living. May (1921)	Nominal wages. (1921)	Real wages. (1921)
Men ...	167	190	114
Women ...	167	173	104
Big lads & Children.	167	192	115
All work people. ...	167	187	112

(Real Wages Index number = $\text{Money Wage Index} \times 100 \div \text{Cost of Living Index.}$)

On account of certain limitations of the cost of living index numbers and other practical difficulties, a similar estimate of nominal and real wages was not attempted by the second enquiry of 1923. A third enquiry was held in 1926, but its results have not yet been published.

The following table shows the variation and the gradual decrease in the cost of living index for the Bombay City since 1920.

Percent increase over July, 1914 (100).

Year	*Cost of living index number	Year	Cost of living index number
Annual average 1920 (October)	193 (High water mark)	1925	155
1921	173	1926	155
1922	164	1927	154
1923	154	1928(July)	146†
1924	157		

LABOUR LEGISLATION IN INDIA.

§ 27. Growing scope of Labour Legislation in India:—Labour legislation in India naturally does not occupy the same important position as in the Western industrialised countries like England and The United States, owing to “the deliberateness of the spread of mechanical power and narrowness of the area affected” ¶ Much of the work is done out of doors or in sheds without walls, and the problems of overcrowding, bad ventilation and undesirable mixing together of the two sexes have not to be faced on the same scale. With the growing industrialisation of the country, a better realisation of the duties of the state towards labour, the awakening of the working classes in India to their rights in recent years and the acceptance by India of her obligations towards the International Labour Organisation of the League of Nations, labour legislation is coming to occu-

* The cost of living index number includes the following articles:—
(i) *Food*: cereals, pulses, other articles of food; (ii) *Fuel and Lighting* ;
(iii) *Clothing*, and (iv) *House Rent*. The articles have been given the relative importance which each bears to the total all-India aggregate expenditure. No allowance is made for any changes in the standard of living since July 1914.

† Labour Gazette, June 1928, p. 826,

¶ Kelman, op. cit., p. 17.

py a more and more important position. And this is as it ought to be. We have already uttered a warning that the spread of big capitalistic industry is attended with certain very serious evils and the state must take action betimes to avoid them as far as possible. We are so impressed with the paramount necessity of state action in this connection that we should be prepared to support it even if it leads to a certain slackening of the pace of industrialisation. It is to be regretted that we have, in some respects, failed to profit by the experience of European countries and have preferred to begin the world afresh, so to speak, and repeated the blunders of other nations who have gone ahead of us in industrialisation. Without the excuse of ignorance we have allowed to appear certain familiar abuses, such as the rise of slum-cities, the exploitation of child labour, excessively long hours of work for men and women, bad sanitation and absence of safety measures—abuses which we are now trying painfully to correct.

The scope of legislation attempted at first in order to remedy these evils was somewhat narrow. Recently, however, with the growth in the numbers employed, the necessity of bringing conditions up to the requirements of international standards and other reasons referred to above, there has been a tendency to extend the scope of such legislation.*

§ 28. Beginnings of Factory Legislation in India:—The question of Factory Legislation in India appears to have been first raised in the Report of Major Moore, Inspector-in-Chief of the Bombay Cotton Department in 1873. About the same time, Mr. J. A. Ballard, Mint Master, Bombay, called attention to the necessity of a Factory Act to restrict the hours of work for women and children in Bombay. The progress made by the Bombay Cotton Mill Industry aroused the jealousy of the Lancashire manufacturers, and in 1874 the Manchester Chamber of Commerce sent a deputation to the Secretary of State for India to urge the application of the British Factory Law to India.† The

* See Broughton : *Labour in Indian Industries*, pp. 153-154.

† Das: *Factory Labour in India*, p. 172

result was the appointment of a Factory Commission by the Government of Bombay in 1875, of which the first Factory Act of 1881 was the outcome. Its main provisions were as follows:—

The employment of children below 7 was prohibited. Between that age and 12, they were not to work for more than 9 hours a day. An hour's daily rest and four holidays in the month were prescribed for children. No relief, however, was given to women and adult male labour. The Act applied to the factories employing not less than 100 persons and using power. Local Governments were to appoint Inspectors of Factories.

Agitation to amend the first Factory Law began almost immediately after its passing. The 1881 Act was on the whole a triumph for conservative opinion, which prevented its provisions from being more stringent as desired by the Government of India and the Bombay Government. The Bengal Government, the Bombay millowners, and the Bombay and Bengal Chambers of Commerce were opposed to any legislation whatsoever; but again pressure from England resulted in the Secretary of State moving in favour of the expeditious adoption of more rigorous legislation and the second Factory Act of 1891 was passed. Its provisions applied to all establishments using power and employing not less than 50 persons. But the Local Governments were to have power to extend it to others employing not less than 20 persons. The lower and upper age-limits for children were raised to 9 and 14 respectively. Their hours of work were limited to 7 in any one day and had to be between the hours of 5 A.M. and 8 P.M. Restrictions were placed on the employment of women. They were not to work in factories before 5 A. M. and after 8 P. M., except in places where an approved system of shifts existed. Their hours of work were limited to eleven in one day entitling them to a total rest of one and a half hours. Men workers were to enjoy an interval of half an hour's rest between 12 noon and 2 P. M. and a weekly day of rest. Certain provisions also secured better ventilation and cleanliness in factories and prevented overcrowding in them.

§ 29. Factory Act of 1911 :—The Cotton Mill industry was expanding rapidly and labour was not so cheap as it had been.

This naturally led to attempts on the part of the employers to get the last ounce of work from the labour that was available. Excessive hours of work were also made possible by the increasing use of electric lights in the Bombay Mills, where in many cases the operatives were being worked for fourteen and a half hours a day. So also a few Calcutta Jute Mills worked their hands for twelve hours and some operatives had to attend for as much as fifteen hours. This gave a handle to the usual agitation on the part of Lancashire manufacturers, and a small Textile Factories Labour Committee (the Freer-Smith Committee) was appointed in 1906, followed shortly after by a Commission which reported in 1908.* The matter was also taken up by the press in India, and it is only fair to add that a leading part in the movement for the reduction of hours of work was taken by some of the enlightened employers. The result of all this agitation was the passing of the Factory Act of 1911 which brought within its scope seasonal factories working for less than four months in the year. It made the possession of an age certificate compulsory. The hours of work for children in textile factories were reduced to 6 per day. The Act restricted the employment of women by night allowing it only in the case of cotton ginning and pressing factories. For the first time the hours of adult male workers were restricted by law, the limit being 12 hours per day in the case of textile factories alone, as recommended by Dr. T. M. Nair, who was the only member of the Factory Commission of 1908 to plead for the direct limitation of hours for adults. Furthermore, in all textile factories, except those working with an approved system of shifts, no person was to be employed before 5 A. M. or after 7 P. M.—the new limits laid down generally for the employment of women and children. Lastly, more extensive provisions relating to health and safety were introduced and factory inspection was made more effective.

§ 30. Factory Act of 1922:—The circumstances that led to the passing of the comprehensive Factory Law of 1922 may be briefly noticed. The great War had important effects on factory

* For a detailed discussion of the recommendations made by the Commission and the vigorous Minute of Dissent by the late Dr. T. M. Nair, see Clow, *Indian Factory Legislation*, pp. 39-45.

administration and ultimately on the Factory Law. There was a considerable extension of industrial activity in India and the number of factories and of persons employed rose by about 25 per cent between 1914 and 1919. Factories had to be exempted from many provisions of the Factory Act and there was a fall in the average number of inspections. But the most important effect was produced on the workers. The increased demand for labour strengthened their position, while the rising prices and profits and the general unrest which followed the War led to increased consciousness of power and a strong disinclination to accept disagreeable conditions. Thus for the first time in India the desire of the operatives became a potent force in securing improved conditions and more drastic legislation.* Moreover, certain defects in the Act of 1911 which, for instance, exempted cotton ginning and pressing factories from all restrictions on female labour led to great abuses. The Indian Cotton Committee strongly condemned this exemption and also the exclusion from the Act of factories employing less than 50 persons. The Industrial Commission of 1918 also referred to the growing volume of opinion in favour of a ten hours day and recommended the examination of the question of reducing the existing maximum factory hours. Lastly, the influence of a new world-wide organisation, viz., the International Labour Organization, was also beginning to make itself felt. The Washington Conference of 1919 discussed several questions relating to labour, such as the eight hours day, night work for women and young persons, the employment of children, maternity benefits and industrial diseases. Mainly as a result of the efforts of the Indian representatives at this Conference, several Conventions contained special provisions which brought them within the sphere of practical politics so far as India was concerned. The acceptance by India of her obligations necessitated further changes in factory legislation, which

* See Clow : op. cit. p. 57.

† A very good illustration of the power acquired by the working classes is furnished by the successful strike of 1920 of the Bombay textile workers for securing a reduction of the hours of work from 12 to 10. A similar concession was won by the workers in Cawnpore.

were effected by the Factories Act of 1922. By this Act, all power-using factories employing not less than 20 persons became subject to factory legislation. Also, option was given to the Local Governments to extend it to factories employing not less than 10 persons whether power was used or not. The minimum age of employment for children was raised to 12 and the upper limit to 15. Children between these ages were not to work for more than 6 hours a day in any factory. Children and women were not to be employed in any factory before 5-30 A.M. and after 7 P. M. The hours of work for adults were limited to 60 in a week and 11 in any day, a week consisting of not more than 6 days. Liberal rest intervals were also secured to all classes of workers. The Act provided for a rest period of an hour after every six hours, though this might be split up into two half hours at the request of the employees, provided not more than 5 hours' continuous work was done. The system of inspection was further improved by the appointment of more whole-time Inspectors with good technical qualifications, in the principal industrial centres. Lastly, provisions regarding safety and health were further extended, the Local Governments being given power to fix standards of ventilation and artificial humidification.

§ 31. Amendment of the Factories Act of 1922:—*The Factories Act of 1922 was amended in 1923 and 1926. The amendment of 1923 removed a minor defect relating to weekly holidays. The later amendment was concerned with certain administrative difficulties which had arisen in regard to the provision for the rest intervals which could not be enforced in some industries without inconvenience to workers or employers. The new Act of 1926 met the difficulty by a provision allowing the reduction of the interval to half an hour for men working not more than 8½ hours a day, provided the men concerned wanted the reduction and the Local Governments granted their sanction. Other amendments recommended by the Conference of Chief Inspectors of Factories were also introduced. Local Governments were authorised to prohibit the cleaning of machinery in motion and to secure better reporting of accidents. Another amendment

* See Clow, *op. cit.* pp. 64-70.

made it an offence for a parent or guardian to allow a child to be worked in two or more factories on the same day---a temptation especially increased at such centres as Ahmedabad with every diminution of hours of work for children and every successive addition to the minimum age of employment; for the one reduced the earnings of children and the other increased the scarcity of child labour. The introduction of a 10 hours day for adult labour by the Act of 1922 in practice reduced the hours of work for children to 5 daily, and the old abuse assumed an aggravated form. The definition of factory was extended so as to include electrical generating stations and water-works.

§ 32. Labour Legislation for Mines:—Labour regulation was much tardier in coming in the case of the Mining Industries than in that of the Textiles. In 1901, the first Indian Mines Act was passed and Inspectors were appointed. In view of the recommendations of the Washington Conference and the large numbers employed in the rapidly developing Mining Industry, the Government of India introduced revised legislation in 1922, which was passed in 1923. It enlarged the definition of a mine, limited the hours of work to 60 per week for workers above ground, and 54 for workers under ground. A week was not to consist of more than 6 days. No child was allowed to work below ground and a child was defined as a person under the age of 13 years. No restriction has yet been placed on the employment of women underground in spite of Mr. N. M. Joshi's plea for prohibition of such work. In view of the fact that 45 per cent of the labour employed below the ground is composed of women, it is clear that sudden and absolute prohibition would cause serious dislocation in one of the basic industries of the country. On the other hand, the need for reform is equally clear. Government have recently prepared a draft scheme for gradually reducing the number of women under ground in coal mines (and also salt mines). This has been received lukewarmly by the representatives of the larger coal mines and has met with the strong disapproval of the smaller owners, who have not hesitated to put forward the absurd contention that labour in coal mines is healthful and easy. The real argument in favour of female labour is of course its

relative cheapness, docility and regularity. There is also the further consideration that the working unit in many of the mines is the family and so the prohibition of female labour would involve a diminution in the male labour supply. At the same time, if the reform is introduced gradually no particular inconvenience need be caused to the coal miners. Further, the increased efficiency of men which may be expected to follow the elimination of women, the introduction of regular shifts and the greater use of labour-saving appliances will minimise and may possibly overbalance the immediate disadvantages. *

The Indian Mines Act of 1923 does not place any statutory limitation on the daily hours of work. An amendment is, therefore, contemplated so as to limit the daily hours of work in mines to 12 and to require, where a mine is worked continuously, that work shall be carried on by a system of shifts. A Bill was introduced in the Assembly in March 1927 and referred to a Select Committee in February 1928. The report of the Committee was submitted in March, 1928. It favours the ultimate adoption of a compulsory 8 hours' shift when the miners have acquired improved habits of punctuality and application under the 12 hours' shift system. For this purpose it is also recommended that the situation should be reviewed after the present Bill has been in operation for three years. The Minority, including Mr. N. M. Joshi, favour an immediate restriction of the maximum daily hours to 8, since the industry is well established having been in existence for the long period of 50 years and the question has been discussed from every point of view for no less than five years.

§ 33. Workmen's Compensation Act of 1923:—Owing to the increase in the number of large-sized industrial establishments and the growing complexity of machinery, the question of compensating workmen against industrial accidents has become an important item of labour legislation. The aim of compensation is to provide the workmen with a substitute for the personal care of the employer which has disappeared under modern condi-

* See the Annual Report of the Chief Inspector of Mines in India, 1927-28.

† Labour Gazette, pp. 887-386,

tions, and to mitigate the effects of accidents, which to some extent are inevitable, by ensuring to the workers pecuniary compensation for the loss of actual wages and earning capacity. The humanitarian aspect of compensation is not its only basis. Economically it is justified, because the knowledge that they are insured makes the labourers better and more contented workers. The right of the worker to be insured at the expense of the industry for all accidents in the course of the worker's regular employment and as a result of the risks taken in that employment has received legal recognition in most Western countries. Legislation in this connection has the effect of increasing the importance in the eyes of the employers of providing adequate safety devices and reducing the number of accidents in a manner that cannot be achieved by official inspection. It also encourages employers to provide adequate medical treatment for their workmen. The benefit so conferred on the workmen added to the increased sense of security which they feel, renders industrial life less unattractive and thus increases the available supply of labour and its efficiency.

The progress of the idea of compensation for accidents has been slow in India. As far back as 1884, workers in Bombay made a demand for the introduction of compensation. Although a certain number of enlightened employers instituted a system of compensation for their workpeople, the practice was by no means generally adopted. Prior to the Act of 1923, an employer could be sued under the Fatal Accidents Act of 1885 in the case of death arising from an accident. But this act was seldom invoked. Further, with regard to the general question of employer's liability the position in India was vague. The object of the original Bill was to make clearer the employer's liability should a workman decide to sue his employer in Civil Court and secondly, to devise a simple and easy method of securing payment to workers of compensation without the matter necessarily being taken to court. The first part, however, relating to the employer's liability in general was dropped and only the second retained. The legislation is admittedly experimental. Very few data are available with regard to industrial accidents and employers are faced with risks which it is difficult to compute. At the same

time the acceptance of the principle that workers are entitled to compensation is a great step in advance.

The principle of the new Act is that compensation should ordinarily be given to workmen who have sustained injuries by accidents arising out of and in the course of employment, compensation being also given in certain circumstances for diseases. Although the measure follows in general principles the legislation in force elsewhere, it also strikes a certain distinctive note and is adapted to meet the peculiarities of industrial life in India. The Act applies to all workers under the Factories Act of 1922 and the Mines Act of 1923, transport workers on railways, tramways, certain classes of workers on ships, dock labourers, certain classes in the building trade, telegraph and telephone linesmen, and underground sewage workers. The scale of compensation is based on the average wages of which the worker was in receipt before the accident. In case of fatal injury, the dependents of the adults, that is to say, of persons above 15, are entitled to much heavier compensation than the dependents of minors, compensation in the former case being the equivalent of 30 months' wages, subject to a maximum of Rs. 2,500, while in the case of a minor, only Rs. 200 has to be paid. In case of complete disablement for life, the adult workman gets 42 months' wages, and the minor workman for twice as long a period, viz, 84 months, subject in each case to a maximum of Rs. 3,500. In the case of temporary injuries, adults receive one-half wages and minors two-thirds. No compensation is to be paid on account of the first ten days of disablement. The general administration of the Act and the settlement of disputes thereunder are matters entrusted to special commissioners with wide powers. The procedure is every simple and opportunities for appeals restricted. For the success of the measure rapid inquiry made by medical men capable of forming estimates of the injuries received, along with the enlistment by the State of impartial judges to see that the worker gets the benefit that is due to him, are necessary. There are several factors which render the operation of a measure of this kind difficult in India. One is the migratory habits

* For the full text of the Act see Labour Gazette, April 1923.

of the industrial labourer. Secondly, the ordinary workman is not in a position to enter into expensive litigation, nor is there any organisation to assist him in seeing a protracted case through. Generally also, the workman is not aware of the financial relief to which he is entitled under the Act. There is further a great lack of qualified men to put up the workman's case properly for compensation. Nevertheless, the measure is generally recognised as one for which there was a real need, and according to the Annual Report of the Government of India for 1926-27, it has been working smoothly, and there has been a marked increase in the number of claims made under the Act and in the amount of compensation paid by the employers. Some labour organisations also, as in Bombay, are assisting workmen to put forward their claims under the Act, though matters are capable of much improvement in this and other respects.

§ 34. Importance of Industrial Harmony :- Industrial prosperity depends upon full and hearty co-operation between workers and capitalists, who have been well called "the two co-efficients in a joint result." Maintenance of harmonious relations between them is, therefore, a matter of the greatest importance. Frequent stoppages of work owing to differences between labour and capital are obviously injurious to both the parties to the dispute. In the course of a prolonged strike huge losses have to be incurred by the employees and apart from the irreparable loss of actual wages, enormous sums of money collected from the workers are uselessly squandered. The tragic part of most strikes and lock-outs lies in the fact that when finally an agreement does come about it is generally on the basis of suggestions made in the very beginning of the dispute. Nor is the loss and suffering confined to workmen and employers alone. The disorganization of production often causes the most serious inconvenience to the general public also as, for example, in the case of public utility services like railways. The great truth that, in the last resort, the interests of labour and capital coincide cannot be emphasised too often. But even with a fuller realisation of it than obtains at present we cannot hope that industrial warfare will cease altogether. For although it is perfectly true that since the interest of both labour and capital lies in efficient and unhampered produc-

tion, they ought to refrain from any action that is likely reduce the total volume of production from which ultimately the reward of each is derived, the proportion in which the division of the wealth produced should take place between labour and capital will always admit of a sharp difference of opinion.¶ The governing idea of Trade Unions is that there is at bottom an irreconcilable conflict of interest between labour and capital, that fair wages and tolerable conditions of work can only be secured by force, and that, therefore, labour's safety lies in the development of the utmost possible fighting strength. Latterly also communistic ideas have been filtering into many countries from Russia and tending to unsettle labour still further, and even India has not been free from the infection.

§ 35. History of industrial disputes in India :—There were a few strikes in this country in the eighties of the last century but on the whole, before 1927, strikes were rare phenomena in India. It was only in the opening years of the present century that the value of the strike as a weapon may be said to have received general recognition. Thus in 1905, there were several strikes in Bombay owing to the introduction of electricity and excessively long hours of work. It was, however, during the War that the strike came to be regarded as an ordinary weapon of industrial warfare. The economic upheaval and the general feeling of unrest created by the War, the increase in the cost of living due to rise in prices and the spread of class consciousness have produced a large crop of strikes since 1917. The position became especially acute in 1919-20, when a great strike occurred in Bombay involving 150,000 cotton mill workmen. Among the contributory causes of these strikes have been long hours of work, bad housing, lack of provision, till recently, for compensation for injuries received, the ill-treatment of the workers by foremen and the sympathy of one group of strikers for others and so on. We shall

¶ For an interesting plan of obviating differences between labour and capital by definitely fixing the remuneration of the latter and making labour the residuary legatee instead of capital, see Oscar Newfang's "*Harmony between Labour and Capital*."

notice in a later section how the Trade Union Movement originated during this period.

§ 36. Frequency of Industrial Disputes:—Statistics relating to industrial disputes in India have been available since the Government of India created a Labour Bureau in 1920, which collects information on labour conditions, keeps in touch with similar organisations in other countries, and systematically gathers statistics regarding strikes, lock-outs, wages, and cost of living. The Labour Office in Bombay does similar work for the Bombay Presidency.

The following statistics show the frequency of strikes in India in recent years:—

Year	No. of strikes.	Year	No. of strikes
1920	200	1924	132
1921	400	1925	134
1922	280	1926	128
1923	214		

These figures clearly prove that the strike is being used as an ordinary weapon of industrial warfare in India. The strike situation was very serious in 1919–1921 owing to the economic distress and high prices induced by the War. With the gradual restoration of normal conditions and a fall in the cost of living, the strike fever appeared for some time to be subsiding. The increased wages granted during the War remained as they were for some time after the War in spite of a fall in prices, thus securing some increase in the real wages of labour (See table on page 140). The trade depression of the last few years, however, has led to a movement on the part of employers of labour to stop paying war bonuses or to decrease wages. This has led to a fresh outburst of strikes at industrial centres like Bombay and Ahmedabad. Thus in 1923 (April–June), there was a large strike in the Ahmedabad Mills involving 48,000 men following

a reduction in wages. Early in January 1924, the decision of the Bombay millowners not to give the annual bonus owing to depressed trade conditions led to a general prolonged strike involving, 160,000 workers. Also, in September 1925, there was a big strike in the Bombay mills involving 1,25,000 men as a result of the decision of the millowners to reduce wages by $12\frac{1}{2}$ per cent, unless the Cotton Exise was removed or suspended. The Cotton Excise *was*, as a matter of fact, suspended in December 1925, which brought the strike virtually to an end. The years 1926 and 1927 were comparatively quiet. The present year (1928) has, however, seen, a recrudescence of industrial unrest, and several big strikes have occurred during the last six or seven months in a number of the organised industries all over the country. The intensification of these striks as well as the unusually prolonged duration of some of them have been attributed to Russian Communistic influences and the secret help derived from the same quarter. The Public Safety Bill, recently thrown out by the Assembly (Sep., 1928), was justified by Government as a necessary measure for nipping in the bud these unwholesome influences. The big strike in the Bombay cotton mills, which has just ended (October 1928), and which began in April last involving 155,644 workpeople, originated in an attempt on the part of the millowners to introduce new methods of work in accordance with the recommendations of the Textile Tariff Board. This occasioned great discontent amongst the workers, partly on account of the additional work which it invloved and partly owing to the retrenchment of hands which was made possible by it, resulting in unemployment. * Several issues such as the standardisation of wages, fines, notice of dismissal, hours of work etc., have been raised in the course of this prolonged dispute. By an agreement reached between the millowners and the Strike Committee, it has been decided to refer the outstanding differences to a Committee of Enquiry consisting of three members appointed by the Government of Bombay. A similar prolonged strike which has just terminated occurred at Jamshedpur landing the Tata Steel Co. into heavy losses. Strikes on several Railways, threatended or actual, and accompanied, in the case of the E. I. R. and S. I. R. strikes, by consider-

* Labour Gazette, Bombay, May 1928 p.752.

able violence have been a feature of the current year. There has been a threat of a general strike on the G. I. P. Railway, the main reason being the introduction of a system of triennial medical examination of all workers employed in the workshops after they have reached the age of 45. Strikes of lesser magnitude but sufficiently important notwithstanding have occurred in the woollen mills at Cawnpore, among the jute mill workers and municipal sweepers of Calcutta, and in the cotton mills of Sholapur.

§ 37. Prevention of Industrial Disputes:-Before dealing with the machinery for the settlement of industrial disputes *after* they have broken out, a few words might be said regarding the methods of preventing them. The first essential is the creation of sound organisations both of employers and employees. The employers are for the most part sufficiently well organised in India, but not so the workers. The formation of sound Trade Unions of the workers is the first step in the evolution of any means, preventive as well as curative of strikes and lock-outs. Efficient organisations on either side, competent to speak for their respective sides, will tend to prevent the occurrence of sporadic strikes and lock-outs and the formulation of grievances *after* rather than *before* going on strike-features which are peculiar characteristics of strikes in India at the present moment. The Bombay Industrial Disputes Committee of 1922, recommend the formation of Works Committees or Shop Committees on the lines of the Whitley Committees in England. On these Committees the workers would be represented along with the employers and would be responsible for the determination and observance of conditions under which work is carried on. Such committees possess the advantage of discounting the absence of personal relationship between the operatives and the employers, and have further an educative value for the operatives themselves. It may be mentioned that such committees have already been established by some enlightened employers like the Tatas and by Government in their capacity as employers. The Industrial Disputes Committee also advocate the extension of the large group of humanistic activities known as welfare work * with a

* See Report of the Bombay Industrial Disputes Committee, 1922.

view to promote contentment among workers and inculcate a sense of common responsibility among them.

We may now proceed to discuss the *arbitration and conciliation methods for settling industrial disputes*. The numerous disputes of the last ten years have clearly shown the necessity of a suitable machinery for investigating and settling them. By way of noting previous attempts in this direction we may mention that the Government of Madras took the lead in setting up Courts of Enquiry to deal with individual disputes as they arose.* A committee appointed by the Bengal Government in March 1921 recommended the institution of Conciliation Boards, the members of which were to be recruited from panels kept by the Local Government being thoroughly representative of all the interests involved. The Boards were to be confined, to start with, to public utility services. The Industrial Disputes Committee appointed by the Bombay Government and presided over by Sir Stanley Reed presented its report in 1922. The Bengal and the Bombay Committees did valuable spade work and made a number of detailed recommendations regarding the machinery to be set up for preventing and settling disputes. These recommendations have served as a foundation for the several Industrial Disputes Bills that have been proposed from time to time. The suggestions of the Bombay Industrial Disputes Committee were considered by both the Governments of Bombay and of India. The big Bombay Mill strike on the bonus dispute early in 1924, led the Bombay Government to expedite matters and prepare a draft Bill to be introduced in the local Council. The Government of India, however, did not allow the Bombay Government to proceed with their Bill, as they considered that the subject was one for all-India legislation. They themselves published a draft Bill in September 1924 for early introduction in the Assembly. The Bill was, however, held up, and the Viceroy declared at Calcutta in 1925 that it would be premature to proceed with this legislation until the Trade Union Bill had been passed. The Trade Union Bill became law in 1926 and came into force the next year. The recent prolonged strike in Bombay made the Government of India anxious to take up the question in earnest.

* India in 1922-1923, p. 209.

The text of the latest Trade Disputes Bill was published in August, 1928 in deference to representations of the Bombay and Indian Chambers of Commerce, to expedite the course of legislation.

§ 38 Trade Disputes Bill of 1928:—The Trade Disputes Bill closely follows the English legislation on the subject and does not provide for *compulsory* arbitration. As in England, public opinion is regarded as the decisive factor in settling disputes; and the underlying idea of the Bill is to help the clear framing and discussion of the issues by an impartial tribunal, so that a well-informed public opinion may be formed. The Bill contemplates the setting up of Courts of Enquiry and Conciliation Boards.

(a) *Nature of inquiry* :—The bill authorises the Provincial Governments or the Governor-General-in-Council, where the employer is the head of a department under the Governor-General-in-Council or a Railway Company, to refer any matter appearing to be connected with or relevant to a trade dispute, actual or apprehended, between the employer and his employees, to a Court of Enquiry or a Board of Conciliation for prevention or settlement of such a dispute. (b) *Constitution of the Court of Enquiry* :—The Court of Enquiry is to consist of a Chairman and such other persons as the appointing authority may think fit, or it may consist of a single person (who presumably will have no personal interest in the dispute). (c) *Board of Conciliation*—The Board of Conciliation will have a different constitution and will consist of a Chairman and two or four other members as the appointing authority thinks fit, or it may consist of one independent person. The Chairman is to be an independent person, and the other persons are to be appointed in equal numbers to represent the parties to the dispute on the recommendations of the parties concerned. (d) *Procedure*—The duty of such a Board is to endeavour to bring about a settlement after investigation of the merits of the dispute and to do all such things as it may think fit to induce the parties to come to a fair and amicable settlement and give them reasonable time for doing so. In case of failure to bring about a settlement, the Board is to send a full report to the appointing authority setting forth the proceedings and the steps taken

by the Board for the settlement of the dispute together with its findings and recommendations. (e) *Strikes in Public Utility Services*:—The provisions regarding Public Utility Services are among the most important in the whole Bill. Special penalties are laid down for employees in the Public Utility Services, in the event of withdrawal from service without permission or without one month's previous notice. An abettor of an offence of this kind is liable to a heavier penalty. (f) *Illegal strikes*:—There are also special provisions in respect of illegal strikes on the lines of the Trade Disputes Act passed last year (1927) in England. A strike or lock-out is to be regarded as illegal which has any object apart from the furtherance of a trade dispute within the trade or industry in which the parties to the disputes are engaged. A strike or lock-out is also to be illegal if designed or calculated to force the Government either directly or by inflicting hardship upon the community. The sums collected or applied in support of such strikes are, it goes without saying, illegal. Sympathetic strikes are declared illegal by defining a trade dispute within an industry as one which is between the employers and the employees of that industry with regard to employment in that industry alone. The Trade Union privileges of members are protected from being invaded on the ground of a refusal to join such illegal strikes.

It may be noted that the Bill presupposes organisation on the part of the employers and the employees, and, as already suggested, is intended to promote such organisation to check sporadic strikes and arbitrary lock-outs and to help the formulation of grievances before and not after a strike is declared. An important omission in the Bill is the absence of any provision to prevent intimidation. Picketing is not mentioned in the Bill because all picketing is not objectionable and it is punishable under the ordinary law when it becomes intimidation.* The prohibition of sympathetic strikes has been criticized by labour leaders as giving Government the power to declare any big strike illegal, but on the other hand, a general strike like

* The English Trade Disputes Act and Trade Union Act of 1927, although it does not prevent picketing, makes unlawful the watching or besetting of a house or place where a person resides.

the triple strike in England may be a real menace to the community. Like many other provisions of law, therefore, this particular provision cannot be demurred to merely because it is liable to be abused. A more valid criticism would be to point out that, since the strikes that have occurred in India so far bear no parallel to the big general strike in Great Britain, there was no particular necessity, under the present circumstances, for such a provision. Another criticism is directed against the vagueness of some terms in the provisions in respect of illegal strikes which are defined as those inflicting a hardship on the community and coercing Government. A more precise definition of what constitutes hardship on the community and coercion of Government would be advisable. Lastly, the objection is raised that the Bill is one-sided in so far as, while penalising the labourer for leaving a public utility service without notice, it allows the employer to go scot-free for dismissing an employee without previous notice.

It is a matter for regret that owing to the pressure of other legislation Government found it impossible to push through the Trade Disputes Bill in the September Session (1928) of the Assembly as was originally intended. It has, however, been circulated for opinion and is expected to be brought forward in the next session of the Assembly (February, 1929). Legislation has been long overdue and Government should see to it that it is placed on the statute book without any further delay and before another serious strike breaks out, if they wish to escape the criticism that they are in the habit of locking the stable door after the horse is stolen.

§ 39. Trade Union Movement in India:—The Trade Union Movement which plays such an important rôle in the economic life of Western countries is of comparatively recent origin in India, as might be expected in view of the late advent of modern industrialism and the special difficulties, to be alluded to presently, which the Movement has to face in this country.

As the President of the 7th Session of the All-India Trade Union Congress held at Delhi, pointed out, Trade Unions of a kind were not unknown in India in ancient times. With the

changes brought about by British rule, however, the movement took shape on Western lines, with modifications to suit the Indian conditions and instead of the old craft structure we have the industrial structure for the Unions. Labour Unions in India came prominently before public notice on account of the magnitude and frequency of strikes, especially since 1920. Already in 1918, however, Trade Unions were organised in Madras with the help of Mr. B. P. Wadia. From Madras the Trade Union Movement spread to Bombay. The industrial unrest, which may be said to have commenced in 1917, resulted in the creation of a number of labour organisations. These were, however, temporary in character and dissolved into thin air as soon as their immediate object, whether it was increase of wages or any other thing, was fulfilled. They were "little more than strike committees consisting of a few officers and perhaps a few paying members."* This situation has, however, been gradually improving and the remarkable growth in the number of Trade Unions, especially in 1921, shows that the Movement has come to stay. It experienced a slight set-back in the year 1923 owing to a certain improvement in the economic condition of the workers and the consequent diminution in the number of strikes. For the initial stages of the movement the presence of actual economic distress is practically the only bond among the workers which tends to weaken when conditions are more favourable. Latterly the movement has shown distinct signs of recovery and may be further expected to gain in strength owing to the protective influence of the Trade Union Act of 1926 and the emergence of capable leaders like Mr. N. M. Joshi. Moreover, the Trade Union Movement in India has almost from its inception had the advantage of an all-India organization like the all-India Trade Union Congress which has been holding annual sessions since 1920. This together with the Provincial Trade Union Federations in Bombay, Bengal and Madras has enabled the Movement to attain a certain measure of co-ordination of its activities. The passing of the Workmen's Compensation Act should also open a useful sphere of activity to Trade Unions and tend to strengthen them.

* See B. Hurst : *Labour and Housing in Bombay*, p. 101.

The Directory of Trade Unions compiled towards the end of 1925 by the Assistant Secretary, All India Trade Union Congress, revealed the existence of eight Federations and 167 Trade Unions in India. The All-India Trade Union Congress claimed in 1926, that it represented organised workers numbering over one lakh. Not all these unions, however, are equal in strength and vitality. About half of them are organisations either of Government servants or of persons connected with Government employment. Trade Unionism has met with comparatively greater success among Railway and Postal employees, but on the whole it is weak in the great organised Textile and Mining industries, though rapid progress is being witnessed in some important centres like Ahmedabad and Bombay.

§ 40. Difficulties of the Movement in India:-The special difficulties of the Movement referred to above are, in the first place, the floating character of the labour population in many of the industrial centres and the strong agricultural interests of the average labourer which induce him to return to his village after a period spent at a factory. In the second place, the labour force in industrial centres like Bombay and Calcutta is a heterogeneous mass of men speaking a variety of languages and, therefore, not feeling intimately drawn to each other. Where, however, the proportion of emigrant labour is small as in Ahmedabad, The Trade Unions are much stronger than elsewhere. Thirdly, many labourers dislike the idea of regular contributions and Union discipline, and this accounts for the small percentage of men enrolled in any establishment. Lastly, the majority of the workers are illiterate and are, therefore, unable to find leaders from their own ranks. This accounts for a special feature of the Trade Union Movement in India, viz., that it has been largely led by men from the middle classes, professional

* In 1922, there were 22 Trade Unions in the Bombay Presidency with a membership of 57,914. The corresponding numbers for 1928 are 87 and 111,320. Out of these 87 Unions, 41 are in Bombay City, 10 in Ahmedabad and 36 in the rest of the Presidency. There are 6 Federations of Trade Unions in the Bombay Presidency, such as the Central Labour Board, Bombay, the Bombay Trades Council etc. See Labour Gazette, July 1928,

lawyers and others who have not in all cases distinguished between political and economic considerations. Moreover, their interests are divided amongst many Unions and their knowledge of technicalities is very slight. All this stands in marked contrast with the position which Trade Unions hold in England being officered exclusively by the workers themselves. While it is, however, easy to decry the interference of politicians and lawyers in labour movements in India, we must also recognise the value of the pioneer work of the educated middle-class leaders in this connection; and although the ultimate aim ought to be the conduct of Trade Union affairs by the workers themselves, at least for some time to come, it will not be possible to dispense altogether with such outside influence.

§ 41. Trade Union Act of 1926:—A decision of the Madras High court at the end of 1920 giving an injunction restraining Trade Union officials or organisers from influencing the labourers to break their contract with their employers by striking to obtain increased wages, had revealed the necessity of legislation for the protection of Indian Trade Unions. And though it was felt to be advisable to wait till the main lines of Union development had had time to settle themselves, Government were compelled to move in the matter earlier than they desired. In March 1921, Mr. N. M. Joshi, the Labour Member in the Assembly, moved a resolution regarding registration and protection of Trade Unions, whereupon Government in September of the same year circularised the Provincial Governments asking for their views in the matter. On receipt of their opinions, which disclosed considerable diversity of views, a bill was drawn up and again sent to Local Governments for opinion in 1924. It was introduced in the Assembly in August 1925 and became law in 1926.

§ 42. Main Provisions of the Trade Union Act.*—The Trade Union Act which came into force on 1st June 1927, defines the legal position of Indian Trade Unions in definite and precise terms. Under the Act, the registration of Trade Unions is optional, but it confers certain valuable privileges on the registered bodies.

* For the full text of the Act, see Labour Gazette, Bombay, June 1927, pp. 905-906.

denied to those that choose to remain unregistered. The registered Trade Union is required to define its name and the objects for which it is established. It must keep a list of its members and provide for a regular annual audit of its funds which must be spent on certain specified objects calculated to promote the obvious interests of the members. No less than one-half of the office-bearers of a registered Trade Union must be persons employed in the industry concerned. As against these restrictions, the Act grants immunity from criminal liability to all Trade Union officials acting in furtherance of all legitimate objects of the Union. Nor are they liable to be indicted for conspiracy. The Act provides that (1) no suit shall be maintainable in any Civil Court against any officer or member of a registered Union in respect of any act done by him in contemplation or furtherance of a trade dispute on the ground only that such act induces some other person to break a contract of employment or is an interference with the trade, business, or employment of some other person or his right to dispose of his capital or labour as he will; and that (2) no suit shall be maintainable in any Civil Court against a registered Trade Union in respect of any act done in contemplation or furtherance of a trade dispute by any person acting on behalf of a Trade Union, provided it is proved that such person acted without the knowledge of or contrary to express instructions given by the executive of the Trade Union. A registered Trade Union may create a fund for the promotion of the civil and political interests of its members, the contributions however, being on a strictly voluntary basis.

INDUSTRIAL WELFARE.

§ 43. Nature of Welfare Work:—Welfare Work has been variously defined. One definition confines it to the voluntary efforts on the part of employers to provide the best conditions of employment in their own factories. A definition more generally accepted includes within the scope of Welfare Work "all efforts which have for their object the improvement of the health, safety and general well-being and the industrial efficiency of the worker."†

† Presidential Address, All-India Industrial Welfare Conference, 1922.

These efforts may be made by employers of labour, or the State, or the employees themselves, or by social agencies. From one point of view, these activities may be regarded as humanistic aiming at the welfare of the industrial population. From the narrower and purely utilitarian point of view, the so-called 'welfare work' may be regarded as 'efficiency work'. It is not purely sentimental, because it has a direct favourable reaction on the physical contentment and efficiency of the operatives thus helping to counteract the migratory tendencies of Indian labour. * Welfare work may also be considered as a means of developing a sense of responsibility and dignity amongst an illiterate class of workers thus making them good citizens.

§ 44. Divisions of Welfare Work:—Welfare work falls into two broad classes: (a) activities inside the factory or *intra-mural* welfare work and (b) activities outside the factory or *extra-mural* work. As regards *intra-mural* work for improving conditions of work inside the factory, an account of what has already been done by the State and, to a smaller extent, by employers has been given earlier in the chapter.

In the past, welfare work, especially in regard to the proper utilisation of leisure time has received little attention at the hands of employers of labour, and such efforts as have been made have mostly taken the form of providing medical aid, minor educational facilities and housing. It is, however, receiving increasing attention at the present time, owing to the serious growth of industrial unrest. The Social Service League of Bombay was able in 1918, to induce two enlightened mill agents to entrust to it the organisation and management of two Workmen's Institutes for the benefit of operatives working in mills under the agencies of Messrs Currimbhoy Ibrahim and Sons and Messrs Tata and Sons. In 1922, an All-India Industrial Welfare Conference was held in Bombay under the Presidentship of Mr. A. C. Chattetjee, I. C. S. Secretary to the Government of India, Department of Industries. Representatives from six provincial Governments attended the

* See the Bombay Industrial Disputes Committee's Report, Labour Gazette, April, 1922, p. 26.

Conference, which discussed several interesting problems connected with welfare work and was able to effect some co-ordination of work carried on by various agencies at the different centres. The All-India Trade Union Congress has also been directing its attention to welfare work for some time past. In May, 1926, the Government of India asked all the Provincial Governments to collect full information with regard to the steps taken and efforts made to ameliorate the conditions under which the workers live when they are not actually employed. This enquiry was undertaken in response to a recommendation adopted by the sixth Session of the International Labour Conference requesting the various Governments concerned to supply the International Labour Office with up-to-date information regarding the use of the worker's spare time.*

Besides the interest shown by some of the more enlightened employers in Bombay, several employers of labour at the other industrial centres have also instituted welfare schemes for the benefit of their operatives in Madras, Nagpur, Jamshedpur, and Cawnpore. The welfare work carried on by the Buckingham and Carnatic Mills in Madras for several years past is well known. At Nagpur the Empress Mills have entrusted the task of looking after the welfare of their employees to the Y. M. C. A. The Board of Directors of the Tata Steel and Iron Company at Jamshedpur recently put forward the claim that "the attitude of the Company from its earliest days towards labour and its provision of housing, education, welfare, water supply, drainage, hospital, and other public services on a scale unexcelled in India have met with the approval of public men of all shades of thought." At Cawnpore, the British India Corporation have provided for a Welfare Superintendent to manage the two Settlements that have been built to house their workers. So also, some of the municipalities like the Bombay Corporation, Port Trusts and Public Utility Services, especially Railways, have taken certain steps to promote the welfare of their employees. Lastly, several social service agencies such as the Bombay Social Service League started by the Servants of India Society, and similar Leagues in Madras and Bengal, the Sevasadan Society, the Bombay Presidency Women's

* Labour Gazette, Bombay, January, 1927, p. 432.

Council, the Maternity and Infant Welfare Association, the Y. M. C. A., the Depressed Classes Mission Society, the Missionary Societies, are all playing a useful part in the organisation of welfare work both by helping employers of labour and by independent efforts.

§ 45 Items of Welfare Work :—(i) *Education* :—The unsatisfactory position regarding the education of industrial workers has already been noticed.* Some enlightened employers of labour like the Tatas have arranged for the education of the children and adult operatives in day and night schools. The Social Service League of Bombay and the Y. M. C. A. have also done much to promote the education of the industrial workers in schools as well as by provision of reading rooms and libraries. (ii) *Medical Aid* :—The provision of facilities for medical attendance appears to be fairly general in the large and important factories in India, though the needs of female workers are rarely met by the appointment of lady doctors. (iii) *Maternity Benefits* :—In the interest of women workers and their children, Western countries have introduced maternity benefits and prohibition of employment of women for some period before and after child-birth. The fact that women workers in India are also domestic drudges makes similar arrangement here all the more important. The Washington International Labour Conference of 1919 adopted a draft Convention concerning the employment of women before and after child-birth. While India was not expected to ratify the Convention immediately, the Government of India was invited to make a study of the question including the grant of maternity benefits and to report to the next Conference. The inquiries in connection with the report submitted showed that such schemes had been instituted only by a very few employers of labour. The reporting Provincial Governments, however, expressed their willingness to encourage the institution of further voluntary schemes. Additional inquiries made by the Government of India in June, 1924 in conformity with the suggestion of the Assembly, showed that, in the three big organised industries of Bengal, viz., Jute, Tea and Coal, there were

*See Chapter 1, Vol. II above.

several definite schemes of maternity benefits. In the Tea Gardens in Assam, and the Assam Railways and Trading Company, in the Mines of Bihar and Orissa, in the Factories of Bombay, Madras and C.P., there are a large number of these schemes in operation, under which several concessions are allowed, such as grant of leave for varying periods of pregnancy, supply of free milk and feeding bottles etc. Over and above all this, Bombay has also a growing number of Maternity Homes. In her final Report, Dr. Barnes, the lady doctor, appointed by the Bombay Government in connection with maternity benefits to women workers, gives interesting details regarding the maternity allowances granted by the Tata and Currimbhoy Ibrahim groups of mills.* Two months' wages are given as allowance (one month before and one month after confinement) to a woman worker with a service of at least eleven months to her credit, on production of a certificate from a lady doctor regarding the completion of eight months of pregnancy and on her giving an undertaking not to work for a wage anywhere else.

Mr. N. M. Joshi introduced, in the September Session of the Assembly (1924), a Bill to regulate the employment, some-time before and after confinement, of women in factories and mines and on estates to which the Assam Labour and Emigration Act of 1901 applies, and to make provision for the payment of maternity benefits. It provided for the grant of leave six weeks before and after confinement and of maternity allowances by Local Governments from a maternity benefit fund subscribed to by employers of labour. The Bill was, however, rejected by the Assembly on the ground that it was too much in advance of public opinion in India. Mr. Asavale, has introduced a similar Bill in the July Session (1928) of the Bombay Legislative Council and it has already passed its first reading. It was, however, opposed by the employers on the ground that it applied only to Bombay. Government thought that it would be unduly burdensome to owners of small factories and that it would be too expensive to institute the proper machinery for safeguarding against the abuse of the concessions. We thi

* See Final Report of the Lady Doctor, Labour Gazette, Bomb 1922, pp. 31-38.

however, that All-India legislation incorporating the principle of maternity benefits ought to be placed on the Statute Book with the minimum of delay, although we quite realise the necessity of making its provisions somewhat more modest than proposed in the above Bills. (iv) *Recreation* :—The value of recreation hardly needs to be specially stressed. Anything should be welcome that adds a little colour to the life of the worker which for the most part is set in grey. It is also most important to induce the worker to utilise his spare time so that he is kept away from the liquor shop and the bucket-shop and generally to increase for him the attractions of industrial work in the towns and make him less reluctant to settle down permanently at the industrial centres in the interests both of workman and employer. In this connection, the activities of the Social Service League, Bombay, which has organised a Working Men's Institute at Parel and of some enlightened employers like the Tatas and the Buckingham and Carnatic Mills, Madras, deserves special mention. Provision is made for outdoor sports and indoor games, entertainments, such as cinema shows, magic lantern lectures, musical concerts, dramatic performances, wrestling matches, etc. (v) *Housing* :—This question has been already fully discussed earlier in the chapter. (vi) *Co-operative societies* :—As already seen* the indebtedness of the industrial workers constitutes one of their most serious handicaps. The organisation of co-operative societies whose progress is at present impeded by the illiteracy and the migratory habits of most workers is calculated to promote thrift and to save the workers from falling into the clutches of money-lenders. The Social Service League, Bombay, has devoted much attention to this question and has organised several co-operative credit societies among the mill hands in Bombay. (vii) *Grain and Cloth Shops* :—Some mills maintain shops where cheap grain and cloth is sold to the workmen thus preventing them from being swindled by the Bania, though the more elastic credit given by the Bania offers a great temptation to the workers to make his purchases from him, a tendency fostered by the degeneration of some of the mill shops into truck shops. The only satisfactory solution lies in the organisation of

*See Vol. I, p. 354.

co-operative stores. (viii) *Tea shops and canteens*:—There is a very meagre provision of tea shops and canteens though there is an imperative need for proper facilities for obtaining good and wholesome tea and cooked food. There are only a few canteens of the type which have made considerable progress in England under the stress of war production, caste difficulties and the conservatism of women acting as great obstacles. It is important, therefore, to make every effort to overcome these difficulties in order to improve the health and the sobriety of the workman.

Though the progress made by welfare work so far has been on the whole encouraging much yet remains to be done as judged by English or American standards. The American employer pays the highest wages in the world and devotes much time and thought to promoting the efficiency of his labour force. The need for similar welfare work is even more urgent in India than in Western countries for evolving, out of the present heterogeneous, floating and illiterate mass of workers, a stable, contented and efficient labour force which is a *sine qua non* of industrial progress, and an indispensable requisite of success in the modern international competition for industrial supremacy.

CHAPTER V

THE POVERTY OF INDIA.

§ 1. The National Dividend :—There are very few questions in Indian economics on which there is absolute unanimity of opinion. One of its conclusions, however, which commands universal assent is the extreme poverty of the Indian people. Various estimates have been made from time to time of the national income of India, and although they have varied widely, even the most optimistic of them have but served to emphasise the fact that the inhabitants of this country are beset with a poverty for which there is no parallel in modern times in the countries of Western Europe.*

While all these attempts at evaluation of the national income of India have been successful enough in conveying a vivid idea of the grinding poverty of the masses, they cannot be taken as possessing much utility as scientific and exact measurements of the *per capita* income in this country. For, though much industry and ability have been brought to bear on these investigations, the statistical information that is available is still very deficient, and the conjectural element is of necessity unusually large.

The term national income or national dividend is generally taken to mean "that part of the objective income of the country that can be measured in money." "The national dividend is composed in the last resort of a number of objective services, some of which are rendered through commodities while others are rendered direct." (Pigou: *The Economics of Welfare*, p. 30.)† The usual plan is to include under national income those objects

* *India in 1924-25*, p. 237.

† "The labour and capital of the country, acting on its natural resources, produces annually a certain net aggregate of commodities, material and immaterial, including services of all kinds. This is the true net annual income or revenue of the country, or the national dividend." Marshall: *Principles of Economics*, p. 524.

and services which are not only exchangeable for money but those that are actually so exchanged. This broad conception of the national income may have to be adjusted and altered to suit particular objects of inquiry. For example, if we are discussing questions relating to the division of the product of industry, it may be advisable to confine our attention to the home-produced income belonging to home-residents, arrived at by deducting, from the total income arising *within* a country (including income obtained by the brains and direction of people and bodies resident there), any outflow going to owners who are not resident in the country. Similarly, if discussions are proceeding upon such questions as the yield of systems of direct taxation of individuals or the distribution of wealth and scope for savings, we must deduct, from the total, that amount of national income which does not form part of individual incomes, either because it is retained by Companies in reserves and undistributed profits, or it belongs to charitable institutions, clubs, co-operative societies etc., and include only that portion which actually accrues to individuals.† Sometimes it may be convenient to take only material production and the sum of added values, as in the case of the Census of Production in England. As Stamp remarks, however, “when all the different conceptions have been studied, we come back to the fact that the sum total of wages, salaries, profits, and interests presents a fairly comprehensible idea, free from important ambiguities, for ordinary comparative purposes.”*

There are three main methods which may be employed singly or in combination for estimating the national income. § The first method relies on the statistics of income taxation. The Income Tax statistics of British India give information about the earnings of government servants, trading classes, persons engaged in industries and liberal profession etc., who have annual incomes of Rs. 2,000 or over. But the number of people covered by these statistics is naturally very small in a poor country like India. The great majority of the people have not “the mingled pleasure

† See *The National Income* (1924) by Bowley and Stamp, pp. 39-40.

* Stamp, *British Incomes and Property*, p. 416.

§ Stamp : *Wealth and Taxable capacity*, pp. 58-59.

and pain " of paying the income-tax. This method, therefore, cannot be relied upon to any very great extent for computing the national income of India. The second method is that of the Occupational Census. Here again, however, there are great difficulties in ascertaining, with anything approaching accuracy, the incomes of a large number of inhabitants. The statistics of subsidiary or secondary occupations, for example, are very imperfect and inaccurate. The third method is that of taking a Census of Production. For this purpose we have statistics regarding agricultural and mineral production which are fairly complete, but with regard to the valuation of repair work, of the production of fisheries, cottage industries, etc., of transportation charges, (other than rail), of merchants' and retailers' charges and profits, of personal services etc., statistics are far less complete and a good deal of guess-work is necessary. Lastly, the statistics that are collected are not very trustworthy on account of the ill-qualified agency which is employed for the purpose. The clerks and village officials do not necessarily put down only well-ascertained fact. They can be more relied upon for making observations of things that are daily under their eyes, but much confidence cannot be placed in many of the figures supplied by them on matters which do not come under their constant observation. For example, the figures about the value of vegetables produced, or the quantity of fish caught, or the quantity of minerals produced on a small scale must be regarded very doubtful. Again, in the permanently settled areas even this imperfect agency for the collection of statistical data is lacking.*

§ 2. Dadabhai Naoroji's estimate:—We shall now proceed to notice briefly the results of the principal estimates of the national income of India made by different writers so far. The first serious attempt in the direction was that of Mr. Dadabhai Naoroji in his well-known book "Poverty and Un-British Rule in India." This estimate is based on official figures relating to the years 1867-1870. Mr. Dadabhai Naoroji explains the principles he has followed in these words:—"The principle of my calculations is briefly this: I have taken

* Dissenting Minute, Economic Enquiry Committee's Report.

the largest one or two kinds of produce of a province to represent all its produce, as it would be too much labour for me to work out every produce, great and small. I have taken the whole cultivated area of each district, the produce per acre, and the price of the produce; and simple multiplication and addition will give you both the quantity and value of the total produce. From it, also, you can get the correct average of produce per acre, and of prices for the whole produce, as in this way you have all the necessary elements taken into account." Working on this basis he arrives at the figure of £ 277,000,000 as the value of the gross agricultural produce from which he deducts 6 per cent for seed. The balance left amounts to £ 260,000,000 representing "the produce of cultivation during a good season, for human use and consumption for a year." Next, £ 17,000,000 is taken as the value of salt, opium, coal, and profits of commerce. The value of manufactures is put down at £15,000,000. An equal amount is allowed for the annual produce of stock, fish, milk, meat, etc., and £ 30,000,000 is further added for any contingency. All these items add up to £ 340,000,000 and taking the population at 170,000,000, the per capita income for British India comes to 40s. or Rs.20 per head. Mr. Dadabhai then proceeds to show on the basis of jail dietaries and rations for emigrant coolies etc. that this is less than Rs.34 or so which is required for bare subsistence and comes to the conclusion, that "Even for such food and clothing as a criminal obtains, there is hardly enough of production even in a good season, leaving alone all little luxuries, all social and religious wants, all expenses of occasions of joy and sorrow, and any provision for bad season." "It must moreover be borne in mind," he goes on to remark, "that every poor labourer does not get the full share of the average production. The high and middle classes get a much larger share, the poor classes much less, while the lowest cost of living is generally above the average share. Such appears to be the condition of the masses of India. They do not get enough to provide the bare necessities of life."*

Objections were raised to Mr. Dadabhai's estimate on various grounds. The agricultural statistics of India, it was said, as they

* *Poverty and Un-British Rule in India*, p. 31.

were published, could scarcely be regarded as very reliable because they were based on averages, each average referring to a very large area, in which there are many variations of conditions and circumstances. It was also pointed out that Mr. Dadabhai Naoroji had made no allowance for the value of straw, nor had he made any attempt to estimate the value of the increase of agricultural stock and had added only an arbitrary sum for the latter and for other omitted items. Further, it was objected that he had adopted the principle of equally apportioning the value of agricultural produce and manufactures, as ascertained by him from the statistics available, amongst the whole population without distinguishing how many were agriculturists, how many machanics, and how many belonged to other trades and professions, or possessed property, and whose incomes, therefore, were derived directly neither from agriculture nor from manufactures, thus omitting all reference to "railway wealth, Goverment stock, house property, profits of trade, salaries, pensions, non-agricultural wages, professional incomes, and returns to investments, and all other sources from which a man who does not grow food himself may obtain the means of purchasing it." Lastly, it was said that if the income of the people was as low as Rs. 20 per annum and if according to Mr. Dadabhai, the minimum expenditure was about Rs. 34 per head, the question was, how under these circumstances the people of the country managed to live at all. * It was suggested, therefore, that there was something manifestly absurd in the calculation. Mr. Dadabhai writing in reply to the various objections, explained in the first place, why he had omitted any reference to straw and also to such things as grass, cotton seed, and any fodder or other food for animals which he had taken in his tables, and also that portion of the inferior grains which is grown for the food of animals. "The principle to be considered is first, either the whole gross annual production, of the country may be taken (including straw, grass, etc. etc.), and from this gross production, before apportioning it per head of human population, a deduction should be made for the portion required for all the stock or second, all straw, grass, and every production raised for animal

* Dadabhai Naoroji, op. cit pp. 174-176.

food should be left out of calculation, and only the rest of the production which is and can be turned to human use should be apportioned among the human population." Either of these two methods could be adopted, but it would not be correct to include the produce raised for animal use and then not to make the necessary deduction for such use. † In this contention Mr. Dadabhai was entirely right. He also disposes of the objection that people could not possibly be so poor as suggested by his estimate since, as a matter of fact, they did somehow manage to exist, by pointing out that "as the balance of income every year available for the use of the people of India did not suffice for the wants of the year, the capital wealth of the country was being drawn upon, and the country went on becoming poorer and poorer and more and more weakened in its capacities of production." We need not go into the details of the remaining portion of his rejoinder. But we may refer to the position he takes up with regard to the exclusion of salaries and pensions, non-agricultural wages, professional incomes and, in general, all services not embodied in material commodities. The reason which he advances for not including the services is that they are ultimately paid for from the material produce and since the latter is counted, including the services also in addition would lead to double counting. From this he proceeds to the wider generalisation that the annual material production of the country is the only one fountain head and that there are no other sources outside this production from which any individual can derive his share of the National Income.

§ 3. Should Services be excluded? :- This argument has been repeated in essence by Messrs. Shah and Khambata in their recent work, *Wealth and Taxable Capacity of India* on which the authors have spent much labour and thought. Contrary to usual practice, their estimate takes account only of material and tangible wealth and leaves services, or immaterial and intangible goods, severely alone. A good many of the arguments which they have advanced in support of this procedure have been fully considered by eminent economists and statisticians like Dr. Marshall,

† *Ibid*, pp. 178-179.

Pigou, Stamp and Bowley, and while they have been led to exclude from computation *some* of the immaterial services, it has seemed to them that there is a balance of advantage in not omitting *every* kind of immaterial service from consideration. Prof. Shah and Mr. Khambata * have urged certain novel arguments in support of the plan pursued by them. which as matters of principle, appear to use of doubtful validity. For example, it is urged that the services of the professional and other non-industrial classes, are not susceptible of measurement.¶ This, however, does not apply to all such services. Many of them are sold for money, and there is no reason why the prices actually paid for them should not be regarded as a measure of their value, while admitting the validity of such a procedure in the case of material commodities. Similarly, the objections that, the services (for instance, those of domestic servants) are not durable, or that they represent 'abstract benefits', or that they cannot be "objectively visualised" and that, therefore, they should not be reckoned in, appear to be irrelevant and untenable.\$ The real point is that the services about which there is question are wealth-utilities because they satisfy a human desire and serve a human purpose and cannot be had gratis, and, therefore, they should be included just as much as material objects which are similarly bought and sold. This is the only practicable test and it can be applied both to commodities and services. It is objected that on this basis many invaluable unpaid services get left out, but then this is also the fate of free utilities like air, although air satisfies a literally vital human need. Messrs Shah and Khambata fear that by admitting services "into an otherwise precise statistical calculation," we would be unnecessarily adding to the elements of uncertainty. In this connection it may be pointed out that even if we include nothing but the value of material objects, absolute precision is unattainable owing to the presence of gaps in the available statistical data which have to be filled up by drawing upon our imagination,

* It is not clear whether Prof. Shah agrees with his collaborator as regards all the reasons advanced by the latter for excluding the services, but he seems to agree with the conclusion that they ought to be so excluded.

¶ See Shah and Khambata, op cit, p 47.

\$ *Ibid*, p. 36, also p. 47.

and that the degree of precision actually attained in the case of material commodities is also possible in the case of a number of services, i.e., those, which are, as a matter of fact, sold for money. Services have the same significance from the point of view of national wealth and welfare as actual commodities, and there does not appear to be any overwhelming ground for their wholesale exclusion. It is argued that some services are not only not useful in any rational sense of the term but are positively harmful. This, however, applies to certain commodities as well, but on that ground it is not usual to base a refusal to admit them into the calculation of the national dividend, provided these commodities are bought and sold for money. The argument that services are ultimately rewarded from material commodities which constitute the only fund of utilities is also obviously false, because while some human needs are satisfied by material commodities, there are others which are satisfied by various kinds of paid services which are, therefore, additive to the material commodities, both together constituting the total National Dividend. To count the value of a service and then also add to this the value of the object resulting from the service would of course be a procedure open to objection as involving duplicate reckoning. But if we guard against this mistake, there does not appear to be sufficient warrant for the plan of a total exclusion of all services whatsoever adopted by the authors we are criticising. We cannot here deal in detail with all their arguments, but the whole of the reasoning employed by them in this connection seems to us to be fallacious. One of the difficulties in comparing the results of the different estimates of national income in India is due to the absence of uniformity of method. It is advisable that there should be fundamental agreement as to what items are to be included and what items had better be left out. From this point of view we think it is regrettable that Messrs. Shah and Khambata have attempted to establish a precedent which is unsound in principle in their otherwise excellent and laborious study.

§ 4. National Income between 1875 and 1911 :—The next inquiry to be noticed after that of Mr. Dadabhai Naoroji was

undertaken in 1882 by Earl Cromer (then Major Evelyn Baring) and Sir (then Mr.) David Barbour and their results were as follows :—†

Agricultural income	Rs. 350,00,00,000
Non-Agricultural income	Rs. 175,00,00,000
Total income	Rs. 525,00,00,000

Divided amongst 194,539,000 people, which was the figure for the population of that time, the average amount per head came to Rs. 27.

The figure for the agricultural income was arrived at thus:—

Presidency or Province	Value of Gross Produce
Punjab	Rs. 34,15,00,000
N. W. Provinces & Oudh	Rs. 71,75,00,000
Bengal	Rs. 103,50,00,000
Central Provinces	Rs. 21,25,00,000
Bombay	Rs. 39,00,00,000
Madras	Rs. 50,00,00,000
Total	Rs. 319,65,00,000
Add, for India, Burma and Assam	Rs. 30,35,00,000
Total	Rs. 350,00,00,003

We may next notice Mr. Digby's estimate which proceeded on the assumption that Government land revenue bears a definite relation to the outturn, and the percentage between the total outturn and the land revenue was taken at a varying figure arrived at by Mr. Romesh Chundra Dutt and used by him in his *Open Letters to Lord Curzon*. The percentages were as follows :—

In Bengal	5 to 6 per cent
„ The N. W. Provinces	8 per cent
„ The Punjab	10 „ „
„ Madras	12 to 31 „ „ say 20
„ Bombay	20 to 33 „ „ „ 25

† See Digby : *Prosperous India*, p. 366.

Shah and Khambata object to this method on the ground that it is not only untrustworthy but also involves *petitio principii* as "it tries to find out the gross product from the multiplier which itself can only be obtained from the gross product; the result will depend upon what multiplier you select."* We are unable to follow this argument, The multiplier no doubt is found as the result of investigations into a certain number of sample cases, but obviously not all the cases are taken into account and, therefore, we cannot see how an argument in a circle is involved in this procedure.

However that may be, Mr. Digby's calculation yielded the following results:—

Agricultural Income for 1898-99	Rs. 285 crores...£189 Millions
Non-Agricultural Income	
(half of above.)	„ Rs. 143 crores...£ 95 Millions
<hr/>	
Total...	Rs.428 crores...£. 284 Millions

Divided among 24.5 crores of people, which according to the calculations of the Government of India was the probable figure for the population, the average income would on this basis be Rs. 17-8-5. The Census of 1901, however, returned only 23.1 crores as the total population. On this basis the *per capita* income would be Rs. 18-8-11, *in a good year*. For the famine year 1899-1900, Mr. Digby calculated that the income would be as low as Rs. 12-6-0.

Lord Curzon in reply to this and other similar statements worked out his own estimate on the basis of the figures collected for the Famine Commission of 1898, giving the latest estimate of the value of agricultural income in India, which was placed at Rs. 450 crores. The calculations of 1880 had shown the average agricultural income to be Rs. 18 per head and taking the figures of the latest Census for the same area as was covered by the earlier computation it was found that the agricultural income had increased to 20 rupees per head. Assuming that the non-agricultural income had also increased in the same ratio, the average income would come to Rs. 30 per head in 1900 as against Rs. 27 in 1880. Lord

* Shah and Khambata : Op. cit. pp. 66-67.

- Curzon admitted that the data were not incontrovertible, but he pleaded that the figures of 1880 were also to a certain extent conjectural and that if one set of figures was to be used in argument, equally might the other. He also admitted that the advance in economic position revealed by the calculations was not in itself "very brilliant or gratifying." But at the same time they showed that the movement was in a forward and not in a retrograde direction.

Mr. Digby now again returned to the charge and re-examined the question in order to show that Lord Curzon's estimate erred too much on the side of optimism. As regards agricultural income he adopted the same old plan of deducing it from the land revenue. But in the case of the non-agricultural income, instead of assuming it to be half of the agricultural income, he examined a large number of items and came to the conclusion that the total income of the country was 259 million pounds which, divided among a population of 226 million people, gave Rs. 17-4 as the average income per head.

Sir J. D. Rees quotes in his '*The Real India*,' Mr. F. J. Atkinson, to the effect that, between 1875 and 1895, there was an increase in the income per head from Rs. 25 to Rs. 34. In February, 1921, the Hon'ble E. M. Cook declared in the Council of State that following the same method of calculation as was adopted in 1882 and 1901 the *per capita* income of 1911 had risen to Rs. 50. He further pointed out that a more elaborate and less defective method of computation would take the figure up to Rs. 80.*

§ 5 Estimate of Profs. Wadia and Joshi:—*Profs. Wadia and Joshi* have worked out an estimate of the national income of India with reference to the year 1913-14. We may briefly indicate the results of their inquiry. The agricultural production is put down at Rs. 1,072,99,93,282 from which is deducted 20 per cent as the amount invested or set apart for seeds, manure, etc. This gives a net figure of Rs. 858,39,94,626. The authors proceed to remark that this deduction is an underestimate, because it does not take into consideration the exhaustion of the soil which must be considerable in a country like India. If, however, we accept the view that the exhaustion of the soil in India has already

* See Pillai, op. cit. p. 44.

reached its highest pitch long ago and that no further progress in it is possible, we need not regard the deduction of 20 per cent as an underestimate. As regards mineral production the gross value is calculated at Rs. 14,40,95,000 from which 20 per cent is again deducted for depreciation in value and the working cost so far as it affects wages (mineral production having been included in the value of manufactures estimated at a later stage of the calculation). We thus get a net valuation of Rs. 11,52,76,000. Next follows the valuation of various products such as hides and skins, manures, wool, silk, poultry products, on the basis of the assumption that exports of these products amount to 80 per cent of the total production. To this is added the value of the products of fisheries calculated at four annas per head for 275 days for 865,000 persons engaged in fisheries. The final addition is in connection with the valuation of products worked by artisans, and earnings of labourers engaged in trade and transport, at four annas per head per day for 310 days for 18,000,000 persons. All this works out at a total of Rs. 154,29,58,750. The next item dealt with is the valuation of the produce of the live stock. The figures taken in this connection relate to the year 1917-18 and it is assumed that the difference between the number of cattle in this year and that in 1913-14 could not be appreciable. The total annual value of all the cattle is estimated at Rs. 349,05,11,518, from which the value of the services of cattle for agricultural purposes is deducted to prevent duplicate reckoning, seeing that these services were already included in the value of agricultural production as given above. As regards the added value of manufactures, this is arrived at by taking it to be at 1/5th or 20 per cent of the gross total of raw materials (Rs. 204,76,65,000). This gives us the figure of Rs. 40,95,33,000. The authors proceed to make various deductions from the total gross income arrived at by the method described above, and they give the following statement showing the various sums to be deducted from the aggregate national income in 1913-14:—

1. Home charges	£ 20,000,000
2. Investment of foreign capital on behalf of Government	8,000,000

3. Profits on foreign capital invested in India	39,000,000
4. Investment of new foreign capital in India	5,000,000
5. Remittances of money from India on private account by Government officers, European employees in Banks, Joint-Stock Companies, etc.	10,000,000
	<hr/>
	£ 82,000,000
	Rs. 123,00,00,000

The following table thus sums up the results of Wadia and Joshi's estimate :—

*Total Annual Income or National Dividend of British India
in 1913-14.*

	Total valuation in Rupees
1. Agricultural production	858,39,94,626
2. Mineral production	11,52,76,000
3. Miscellaneous products and earnings of artisans etc.	154,29,58,750
4. Produce of live stock	145,10,34,634
5. Manufactures	40,95,33,000
	<hr/>
Total net valuation	1,210,27,97,010
	<hr/>
Deduct for home charges etc.	123,00,000,000
	<hr/>
Net annual income	1,087,27,97,010

Dividing this net income by the total population of British India, viz., 245,189,716, we get as the annual income per head Rs. 44-5-6 or £ 2-19-1.

The population of British India according to the Census of 1911 was 244, 189, 716. To this has been added 1,000,000 as representing the possible increase in numbers in three years.*

* For further details about this estimate read the admirable chapter on the " *The Income of British India* " in Wadia and Joshi's *Wealth of India*, pp. 97-112.

§ 6. Shah and Khambata's Estimate:—Prof. Shah and Mr. Khambata's estimate is summarised in the following table. *

I T E M S	Pre-War period 1900-14	War & post-War period 1914-22	Whole period 1900-22	Year 1921-22
(Figures in Crores of Rupees)				
Agricultural Produce Deduct for seeds	1014.8 -20	1686.5 -35	1257.1 -25	2155.8 -58
Net agricultural Produce	994.8	1651.5	1232.1	2097.8
Forest Wealth	10.0	20.0	14.0	28.0
Fisheries	1.2	2.5	1.9	3.2
Manufactures	80.0	150.0	106.0	186.0
Mineral Wealth	10.0	21.6	14.0	28.7
Buildings etc.	10.0	16.4	12.0	20.3
Total	1106.0	1862.0	1380.0	2364.0

This gives the *per capita* gross income of

{	Rs. 36 for 1900-14
	Rs. 58½ for 1914-22
	Rs. 44½ for 1900-22
	Rs. 74 for 1921-22

Making an adjustment with reference to the change in the level of prices the income is stated at the pre-War average price level as amounting to Rs. 36 per head for the pre-War period and Rs. 38-2 for the War and post-War periods. From the gross income the authors make a number of deductions on account of home charges etc. and come to the conclusion that this "drain" takes about Rs. 7 away from the *per capita* income for 1921-22 reducing it to Rs. 67.

§ 7. Findlay Shirras' Estimate:—The most recent estimate is that made by Mr. G. Findlay Shirras and relates to the years 1920-21

* *Wealth and Taxable Capacity of India*, pp. 199-200.

and 1921-22.* He puts the agricultural income for the former year at 1714,94 lakhs of Rupees and for the latter at 1983,41 lakhs of Rupees, and calculates the non-agricultural income at 883 crores of Rupees. On this basis the per capita income comes to Rs. 107 for 1921, and Rs. 116 for 1922. Mr. Shirras points out that, in all the inquiries between 1881 and 1911, it had been assumed that the gross income of agriculturists and non-agriculturists was distributed between the two classes in proportion to their numbers. This worked satisfactorily enough so long as the country was industrialised only to a small degree. But during the previous few years rapid changes had taken place and some additional allowance was therefore necessary in order to arrive at the total non-agricultural income,† and the addition of Rs. 75 crores appeared to meet the requirements of the case giving the total of Rs. 883 crores. Mr. Shirras goes on to check this figure by utilising other available data, and as the result of a study of the occupation tables in the Census Report of 1921 together with the approximate earnings in each industry, he arrives at the result tabulated on the next page.

The total non-agricultural income of 1019 crores would come to a minimum of 900 crores if an allowance of 10 per cent is made for probable error. Mr. Shirras further tests this figure

* In 1921 the Statistical Branch of the Madras Department published an estimate of the agricultural income in the Presidency which showed that the total agricultural income amounted to Rs. 309.7 crores. The agricultural population in the Madras Presidency is about five-sevenths of the total population, and if it is assumed that the contribution of the agricultural population to that of the non-agricultural population is in proportion to strength, the total non-agricultural income would be two-fifths of the agricultural income. This takes the total income up to Rs. 434 crores. The population of Madras according to the Census of 1921 was 43.3 millions, so that the average income per head works out at about Rs. 100. If allowance is made for the rise in prices between 1899 and 1920 this would correspond to Rs. 42 in 1899, thus showing a real increase in income of 40 per cent. See Pillai, *op. cit.* p. 44.

We may also mention here that according to the Report on an Enquiry into Working Class Budgets in Bombay, 1923, the *per capita* income of the industrial workers in Bombay City and Island was Rs. 146-6-0, which is considerably higher than the average income for the whole Indian population.

† G. Findlay Shirras: *The Science of Public Finance*, pp. 138-145.

Occupations	Number of actual Workers (Millions)	Approximate Annual Earnings per Worker Rs. in crores	Aggregate Annual Earnings Rs. in crores
Industry	15.7	240	375
Mines	.2	180	4
Transport	2.0	300	60
Trade	8.0	500	400
Public Adminis- tration	1.0	150	15
Public Force	1.0	150	15
Professions and the Liberal Arts	2.1	500	100
Domestic services	2.5	200	50
Total	32.5		1019

by adding to the non-agricultural income of British India in the pre-War year (530 crores), the increase of 60 per cent, being the rise in the wholesale index number. This gives 850 crores. All things considered, he concludes, the figure of 883 crores for non-agricultural income in 1920-21 and 1921-22 is not far out. One of the obvious criticisms of Mr. Shirras' estimate is that he makes no deductions on account of seed in computing the agricultural income and this does not seem to be justified by the ordinary practice in this connection. For the concrete content of the national dividend is generally taken to be "the inventory of things made and (double counting being eliminated) services rendered, *minus*, as a negative element, the inventory of things worn out during the year" or consumed in the process of production."* It should further be noted that the non-agricultural income is about 40 per cent of the agricultural income in Mr. Shirras' estimate, whereas it is only about 10 per cent in Shah and Khambata's estimate and about 30 per cent in that of Profs. Wadia and Joshi. This disparity is due, among other things, to the difference in the treatment of the service utilities. We have already seen that Messrs Shah and Kham-

* Pigou: *The Economics of Welfare*, pp. 38-39.

bata exclude the services from their computation, whereas Mr. Shirras includes them and as we have already argued, Mr. Shirras' procedure is the sounder of the two as a question of principle.

We may now present in a tabular form the results of the different enquiries which we have discussed.

Estimates by	Relating to year	Income per head		
		Rs.	as.	ps.
Dadabhai Naoroji	... 1870	20	0	0
Baring-Barbour	... 1882	27	0	0
Digby	... 1898-99	18	9	0
Lord Curzon	... 1900	30	0	0
Digby	... 1900	17	4	0
Atkinson	... } 1875	25	0	0
		34	0	0
	... } 1895	50	0	0
	1911	80	0	0
Wadia and Joshi	... 1913-14	44	5	6
Shah and Khambata	... 1921-22	67	0	0
Findlay Shirras	... } 1921	107	0	0
		116	0	0

§ 8. Difficulties of interpretation and comparison:—In comparing these results the reader must bear in mind several cautions. The first is that they relate to different dates and before a comparative analysis is made of the economic condition of the people as between one date and another and it is desired to find out the direction of the change, if any, the difference in prices at the two dates must be taken into account. Thus, Rs. 45 in 1913-14 would be equivalent to Rs. 81 in 1921-22 on the assumption of an 80 per cent rise of prices. Another fact to be remembered is that the area covered by the computations is not in every case the same. For instance, Shah and Khambata include not only British India but also the Native States, and if a comparison is to be instituted between their estimate and another one which is limited to British India, we should probably have to raise the per capita figure of Messrs. Shah and

Khambata somewhat, assuming that British India is slightly richer and economically more advanced than the Native States taken as a whole. We must further allow for the difference in the methods adopted in the inquiries, more particularly as regards the deductions from the gross income. We have already seen, for example, that Mr. Shirras does not make any deductions, whereas the other estimates make them to a smaller or greater extent. Again, we must remember that there is a difference of treatment arising from divergent views as to the constituent elements in the national dividend. As we have seen above, Mr. Shirras' estimate includes the incomes of the professional classes,* while they are deliberately excluded in some of the other estimates. In order to institute profitable comparisons between the results of inquiries relating to two different periods we must not take the actual figures as they are given, but as they would have been if the methods adopted had been identical. Another point to notice is that, generally speaking, the later valuations are on a more scientific and careful basis; and as Mr. Shirras points out, if the old methods were followed in preference to his more elaborate method the values of agricultural produce and non-agricultural income in his estimates would be appreciably lower. For example, instead of 1983 crores of Rupees as the agricultural income for 1922, we should have the figure of 1529 crores of Rupees; similarly, instead of 889 crores for non-agriculture income we would have to substitute 550 crores, accounting for a total difference of about 800 crores. (Shirras: op. cit. p. 141, Footnote.)

Particular care is also necessary in drawing inferences about economic welfare from the *per capita* income. Here it is important to consider not only the average income per head but also the composition of the national income. In the case of India, for instance, an inquiry as to how much of the national income is in the form of food-stuffs would be specially pertinent. For, if the supply of an absolute necessary of life is disclosed to be

* Mr. Shirras does not explicitly include services in his main estimate but, as already seen, he checks his figures for non-agricultural income by a table in which the valuation of various services, which do not issue in material commodities, is included.

insufficient, additions to the national income in other forms cannot be regarded as of the same order of importance as food-stuffs. Again, if services are included in the computation, the semi-political question whether some of the services are not overvalued in India cannot be ignored.

Lastly, we feel bound to utter a general caution, viz., that in considering the result of any particular inquiry we must take into account the spirit and purpose underlying it. A good many of the investigations referred to above have been admittedly informed by a spirit of political controversy, and are intended as supports to views independently formed regarding the condition of the country and the general drift of events bearing upon it. Generally, therefore, we find that the course of the investigation is interrupted by road-side notices that the particular valuation is a deliberate underestimate or overestimate as the case may be. If these protestations are to be taken seriously and literally, then the final results must be interpreted in their light. That is to say, if the author of a particular estimate declares that his estimate is above the correct figure, then we must reduce the figure somewhat. If on the contrary, we are assured that we are dealing with a deliberate underestimate, we must make a suitable addition. The curious thing, however, is that the pretended underestimates almost invariably give us a higher figure than the pretended overestimates, because liberal concessions granted to rival disputants "for the sake of argument" in one direction are more than made up for by quietly taking liberties whose effect is to swing the pendulum violently in the opposite direction.* Safety for the unsophisticated outsider and the dispassionate student would therefore seem to lie in averaging the highest and the lowest figures.

In spite of the discrepancies in the results obtained by the different investigators one fact which clearly stands out from all of them is the intense poverty of India. Even as regards a prime necessity of life, such as food, a large proportion of people

* Exigencies of political controversy, no doubt, necessitate the adoption of such tactics and they are perfectly legitimate in their proper place. It is not for us here either to praise or to blame but merely to state the facts as they are.

in this country cannot afford to buy the necessary amount of it required for their bare physical needs. The validity of this statement is not affected by the inconclusive evidence to which we have referred as regards the question whether the food supply of the country is increasing in proportion to the increase in population.* Whether or not the aggregate food supply is inadequate and, if so, whether the inadequacy is increasing or not, the fact is beyond dispute, that a distressingly large number of the people are in a semi-starved condition. † Sometimes, however, the picture of extreme poverty gets overdrawn by people arguing as if the *per capita* income were the income of the principal bread-winner of an average family. If the *per capita* income is taken to be, say, Rs. 100, and if we are considering the economic position of an average family of five people, the total resources of the family would have to be regarded as Rs. 500 per year.

But here again, we should be making the mistake of supposing that the condition of the masses is better than it really is, unless we remembered that the national income is very unevenly distributed. Some people enjoy very much more than the average income and some very much less. The learned professions and the bigger landowners enjoy a very much higher income than the cultivators or industrial labourers. The petty traders and shop-keepers have incomes of a medium size. Messrs Shah and Khambata give the following figures to show the uneven distribution of the national income in India. §

“ 6,000 individuals, with an average income per head of Rs 100,000 per annum absorb 60,00,00,000 among them, and support 30,000 persons.

230,000 individuals paying income Taxes with an average income of Rs. (?) supporting 1,150,000 persons.

270,000 individuals escaping or exempted from the Income Tax, but having an income liable to that tax, with an average

* See Vol. I, pp. 90-91.

† Profs. Vakil and Muranjan support the view that the food supply is not only inadequate but that the inadequacy is progressively on the increase. See Vakil and Muranjan: *Currency and Prices in India*, p. 363.

§ Shah and Khambata: *Wealth and Taxable Capacity of India*, p. 307.

income of Rs. 5,000 per head per annum, absorb among them 135,00,00,000 and support 1,350,000.

2,500,000 individuals with an average annual income of Rs. 1,000 absorb among them Rs. 250,00,00,000 and support 1,25,00,000 persons.

35,000,000 individuals with an average income of Rs. 200 per annum absorb among them Rs. 700,000,000 and support 10,00,00,000 persons.

The remainder have an average income of about Rs. 50 per annum and absorb among them 825 crores.

The result of this calculation is that more than a third of the wealth of the country is enjoyed by about one per cent of the population, or allowing for the dependents about 5 per cent at most; that slightly more than another third, about 35 per cent of the annual wealth produced in the country is absorbed by another third of the population allowing for the dependents, while 60 per cent. of the people of British India enjoy among them about 30 per cent. of the total wealth produced in the country."

It should also be remembered that the *per capita* income varies from Province to Province. It would be larger in those Provinces which grow commercial crops and which are relatively more industrialised, such as Bombay, Sindh, the Punjab, Assam, the Central Provinces and Berar, whereas Bihar and Orissa, the United Provinces and Madras are relatively poorer Provinces.

§ 9. International Comparisons :—International comparisons cannot be based merely on a consideration of the *per capita* income of the countries under comparison. Sir Robert Giffen drew attention to the dangers of making these comparisons without introducing the necessary qualifications and of assuming "that figures called by the same names in different countries have exactly the same values."† Figures of the income per head do not tell us much about the economic well-being of the people

* See Vakil and Murajan : op. cit., pp. 356-357.

† Quoted at p. 97 of the Report of the Indian Economic Enquiry Committee, 1925.

of one country as compared to people belonging to another unless we allow for such factors as differences in standards of living, habits and customs. As Sir Josiah Stamp points out "In the countries to be compared men must care for the same objects in a similar way, and their scale of relative values must be akin. To the extent to which countries diverge in this respect, the comparison will be invalid."* The same income per head, for example, would obviously have an entirely different significance in two countries, so wide apart from each other as India and England, because the scale of values is different not only owing to different modes of thinking but also because external conditions impose different standards of requirements. Broadly speaking, owing to the warmer climate of India an appreciably smaller expenditure is required on food clothing, fuel and housing than in England. However, when every allowance is made for these factors to be borne in mind in instituting international comparisons, the following figures are sufficiently eloquent and show the tremendous distance between India and some other countries in economic prosperity.

(i) *Income of the chief Powers in 1914.* †

Name of Country	Income per head in 1914	Name of Country	Income per head in 1914
United States	£72	Germany	£30
United Kingdom	£50	Italy	£23
Australia	£54	Spain	£11
Canada	£40	Japan	£6
France	£38	India	£3

*"It is very doubtful whether numerical comparison can be safely made between two countries ; neither housing, clothing nor food are comparable. The importance of that part of income which is not wages varies greatly, and many things must be bought in one country which are unnecessary or are home-made, home-grown, or obtained freely in another. Nor should we compare industrial classes, such as workmen, engaged in building, engineering or printing, in different countries, since methods and conditions of work vary enormously, unless we make very broad allowances for the possible effects of such variation," A. L. Bowley : the *Measurement of Social Phenomena*, quoted by the Economic Enquiry Committee's Report, p. 117.

†Sir Josiah Stamp, *The Wealth and Income of the Chief Powers*, a paper read before the Royal Statistical Society, May 20th, 1919.

(ii) *Income Per Capita of some of the countries of the World in 1919.†*

Country	per capita income (in dollars)	Country	per capita income (in dollars)
United States	561	Portugal	83
Great Britain (not including Colonies)	337	Greece	12
France	300	Rumania	13
Russia	40	Germany	154
Italy	208	Austria-Hungary	94
Japan	46	Bulgaria	84
		Turkey	42

In 1926 the income of the United States was placed at about Rs. 1,925, that of Britain at Rs. 1,000 per head, Australia and Canada Rs. 550 per head, whereas India's income, as we have seen, has been estimated variously from Rs. 67 to Rs. 116.

§ 10. Intensive Inquiries:—Besides computations of the income per head, various intensive village and regional inquiries have been made by different investigators, such as Dr. Mann in Bombay and Dr. Slater in Madras, and, as might be expected, the results obtained by these inquiries fully confirm the general conclusion regarding the poverty of the masses. For the village Pimpla Soudagar (1917) Dr. Mann works out an income of Rs. 218 per family or an income per head of population of Rs. 43-3-0 obtained in an average good year. The expenditure per family of five persons is given as Rs. 200-8-0 after the payment of *Balutas* and interest charges on debt. To this figure Dr. Mann adds Rs. 11-10-0 in view of the larger proportion of adults in the village than in the ideal family for which the calculation was made. This gives Rs. 42-14-0 per head on the average for the 103 families for whom the records were complete. If *Balutas* are included in the case of cultivators' families (71 out of 103) the total expenditure per head would be Rs. 44. Assuming a normal year and ignoring payments on account of debts, this shows that the cultivators' families with an income of Rs. 44 per head would just pay their way. But, of course, the existence

† These figures are quoted by Comish in *The Standard of Living*, p. 67.

of debt entirely alters the situation and Dr. Mann is brought to the conclusion that "Out of 103 families investigated, only 36, or just under 35 per cent., can pay their way on the standard they themselves lay down. The others are living below that standard, and this conclusion, which seems very clear, forms an exceedingly serious state of affairs." Dr. Mann's study of another village of the Deccan, Jategaon Budruk, led to a similar conclusion. Major Jack's inquiries (1910-14) into the economic conditions in the Faridpur District in Bengal yielded the following results:—

Classified as living	Persons	Income per head (in Rupees)
in comfort	951,205	65
below comfort	524,803	40
above indigence	319,315	33
in indigence	65,860	25
Total	1,861,183	(average income)

Numerous other intensive surveys have recently been made generally corroborating the conclusions as stated above about the economic conditions of the people. Under the auspices of the Rural and Urban Sections of the Board of Economic Inquiry, Punjab, a number of valuable investigations of this kind have been carried out recently. Highly useful work has also been done by several other individual investigators and in this connection mention may be made of Dr. Panandikar's "Wealth and Welfare of the Bengal Delta"; Messrs S. R. Deshpande and G. S. Ghurye's "Some Village Studies" (in the Konkan) and Prof. Keshav Iyengar's "Studies in Indian Rural Economics" (in Mysore). Limitations of space prevent us from taking any detailed notice of these intensive surveys.

§ 11 Is Indian poverty on the decline? :—Granting the existence of appalling poverty as an indisputable fact, the question whether it is increasing or diminishing, or whether there is no movement either way, has been variously answered. Profs. Wadia

and Joshi hold that during the 20 years between 1895 and 1914 the condition of the population has not undergone any change. The more common view, however, is that there has been recently a real, if a very slow, amelioration in the condition of the people. That the people are getting more and more discontented is true, but as European experience shows, this is quite compatible with a great betterment in the economic position of the masses. With increasing wealth there generally comes an increase in the consciousness of poverty. A people may be so brutalized by extreme poverty as to lose all consciousness of it. But a little relief from it is commonly followed by a desire for still further relief. Modern economic advance has been accompanied by a great multiplication of human wants and the modes of satisfying them, so that poverty has come to mean not so much the inability to satisfy a few primal wants but rather the inability to share in the new known goods of each period. Although the masses are better fed, better clothed and better housed to-day in the Western countries than at any other previous period, they are more discontented with their state than ever before. According to some observers, a similar change has come over the spirit of the people in India and this is one of the results of a decided improvement in their economic condition. The official view in this country is that the amelioration is unquestionable and the reasons generally advanced in support of it are well exemplified in the following quotation, "So far as ordinary tests can be applied, the average Indian landholder, trader, ryot, or handicraftsman is better off than he was 50 years ago. He consumes more salt, more sugar, more tobacco, and far more imported luxuries and conveniences than he did a generation back. Where house to house inquiries have been made, it has been found that the average villager eats more food and has a better house than his father, that to a considerable extent brass and other metal vessels have taken the place of the coarse earthenware vessels of earlier times, and that his family possesses more clothes than formerly."* The truth of this picture has been challenged by non-official observers and some of its details especially have been regarded as open to doubt.

* Results of Indian Administration in the past 50 years, Cd. 4956, 1909, p. 26, quoted by Knowles, op. cit. p. 275.

For example, the statement that the average villager eats more food has not been universally accepted. We suggest it as a possibility that the average villager lays out his slightly increased income on a larger number of commodities than before but that he has not been able to increase his standard of diet. Indeed, there are reasons to suppose that in the villages, especially those in the vicinity of towns, the dietary of the average villager has deteriorated and he is worse nourished than before. The average consumption of milk products which occupies such an important position in a purely vegetarian diet has distinctly fallen off and there does not seem to have occurred the addition of any substitute to his diet which can be regarded as of equal nutritional value. This may be due to a relatively higher increase in the prices of milk products than in those of other commodities, and the position with regard to the milk products as stated above is not necessarily inconsistent with the hypothesis of a real increase in the *per capita* income of the people. But there is at least one proposition that can be stated in this connection without fear of contradiction; and that is, that the increase in the wealth of the country, such as it is, cannot be compared for a moment with the amazing advance achieved by some of the foremost countries of the West, in recent times—an advance reflected in fall of pauperism, decrease of death-rate and poverty diseases, increase of wages, shortening of hours of labour, spread and improvement of education, increase in the means of recreation, better housing and sanitation etc. There are indeed great inequalities in the distribution of wealth in the West but there can be no question about the wide diffusion of economic well-being. The cheapness and plenty of the good things of life together with the universal rise of incomes have brought within the reach of the masses many commodities and modes of enjoyment which were formerly the monopolies of the very rich and have resulted in what Vte D'Avenel calls "*Le nivellement des jouissances*" (a levelling up of enjoyments)*.

§ 12 Need for better Statistics :—In pronouncing judgements on the various problems concerning the economic condition of

* Vte Georges D'Avenel : *Decouverts d'Histoire Sociale*, pp. 295-318,

the people in India, it is found that nothing more than a halting, uncertain attitude is possible under the present circumstances for lack of precise statistical information. The only certain conclusion, which as we saw emerges from the investigations made by the various able inquirers referred to above, is that India is intensely poor. But this is a truth which most people have discovered for themselves by the direct evidence of their senses, and to put forward elaborate statistics to prove what is perfectly obvious to everybody is like taking out the candle to look for the sun. On everything else besides the obvious fact of extreme poverty, we are left more or less in the dark. The collection of reliable statistical data will make our information more precise and minimise the large number of conjectural assumptions which are now unavoidable in every inquiry. It will also make possible a correct diagnosis of the numerous economic and social ills from which the country is suffering, and will be of great assistance in tackling the day-to-day problems of administration. The Indian Economic Enquiry Committee (1925) quotes the following apposite remarks of the London *Times* in this connection. Speaking of the Empire Statistics Conference which sat in January and February 1921, it said, : " In Germany before the war the Statistical Bureaux were ceaselessly employed in working on everything that illuminates the future of the German people; and in the era which is now opening there can be little doubt that the nation which studies the drift of events as it is revealed by statistical analysis will be infinitely better equipped to take advantage of its opportunities than another which perhaps trusts only to the methods of empiricism. " * The statistics at present collected are often uncoordinated and without expert direction and are generally a by-product of administration meant more for departmental use than for the purpose of affording information to the public about important social and economic activities.

It is indeed true that in India, the collection of statistics is attended with extraordinary difficulties. In the first place, the huge size of the country makes the enterprise expensive and difficult to carry out. Secondly, the population in India is

* Economic Enquiry Committee's Report, p. 4

scattered in rural areas and not concentrated in big cities and towns. Thirdly, the existence of illiteracy makes the co-operation of the public in the work of gathering statistical data a practical impossibility. In Great Britain and the Dominions, the statistics of production of wages and prices are usually collected by distributing schedules to private individuals who are required to fill them up within a given time and return them. This is both a more accurate as well as a less expensive method than that of engaging a special paid staff. Much assistance is also derived from the co-operation of a number of private associations, the like of which are almost entirely absent in India. Absence of organised enterprise and the existence of numerous small unorganised undertakings further make statistical work extraordinarily difficult.* However, although we cannot hope immediately to attain to the standard of equipment usual in the Western countries, there can be no doubt that the present position in this regard in India admits of very considerable improvement. The Economic Enquiry Committee's Report as well as the Dissenting Note of Prof. Burnett-Hurst contain many useful suggestions as to how this might be done and also as to the scope of statistical inquiry in this country. The Report points out that, while estimates of national wealth and income have their uses, there are other numerous tests of economic condition which must be applied for obtaining a true and complete picture of the economic condition of the country. For example, the cost of living is an important test which must not be ignored and attempts must be made to ascertain it from time to time by means of family budgets or house to house canvass. Again, local and special enquiries of various kinds such as those concerning cottage industries, indebtedness, general condition of villages, conditions of labour in industrial areas are also necessary. Intensive inquiries into the conditions of a village or a district often throw much light upon matters which are not revealed in a mass investigation, *provided the regions selected for inquiry belong to as many different types as possible.*

Among the recommendations made by the Economic En-

* See Prof. Burnett-Hurst's Note of Dissent to the Economic Enquiry Committee's Report, pp, 91-92.

quiry Committee we may mention the following:—(1) A quinquennial review of the data collected from year to year on agricultural production should be taken. (2) A detailed census of industrial production should be taken every five years.* (3) All statistical work should be co-ordinated and centralised, the aim being to provide a common purpose and give the statistics an economic trend by means of a central thinking office. (4) A Central Statistical Bureau should be established presided over by a Director of Statistics and should take the place of the Statistical Section of the Office of the Director-General of Commercial Intelligence for the purpose of centralisation of statistics, particularly those of economic significance. (5) Every Province should have a Provincial Statistical Bureau with a Provincial Statistician at its head and a staff of Assistants, usually one for every revenue division, to supervise the work in the districts, etc.

§13. Causes of Indian Poverty:—The poverty of India is a highly complex phenomenon and the factors accounting for it are varied and innumerable. We have already discussed the view that the poverty of the people is in the last analysis due to a defect of outlook on their part, caused by a religion† which is unworldly beyond any other. People in India, so runs the argument, are too spiritually minded to care sufficiently for the production and accumulation of wealth. They seek to achieve contentment not by increasing standards of living and then by struggling to satisfy these standards, but rather by a rigid limitation of all desire. Rather than add more fuel, they prefer to take away as much of the fire as possible. Other alleged causes are contempt for manual labour; the sufferance or even encouragement of thousands of parasites like the wandering Fakirs and Bairagis who are a burden on the community; the cramping influence of various religious prejudices and the existence of a number of anti-economic customs and traditions such as those, for instance, which result in the

* Prof. Burnett-Hurst, however, is very sceptical about this recommendation. A reliable census of production is a most difficult matter even in advanced countries like England, and according to Prof. Burnett-Hurst, to attempt it in India would be sheer waste of labour. See Economic Enquiry Committee's Report, pp. 94-95.

† See Vol I, Chap. IV.

withdrawal of a large number of women from all economic activities; unrestricted multiplication of numbers; various practices like that of early marriage, which sap the physical vitality and, therefore, diminish the economic efficiency of the race; prevalence of diseases like malaria and hookworm which have the same debilitating influence; the love of litigation which is supposed to characterise the Indian people whose delight in scoring points, it is said, makes the court of law such a haunt for them etc. The administration is also blamed as being in no small measure responsible for the backwardness and the poverty of the country. Government are accused of not having exerted themselves, as much as they ought to have, to develop the economic resources of the country. Particularly are they charged with having failed to take the necessary steps for fostering industrial development. Lastly, the theory of the 'Drain' has served for many people as a sufficient explanation of Indian poverty. Some of these causes have already been dealt with in their appropriate places and others like the Drain will be treated in the succeeding chapters.

§ 14. Some errors of consumption as aggravating causes of Indian Poverty:—Whatever tends to reduce the productivity of the people must be regarded as a cause of poverty. But besides low production unwise consumption may also act as a drag on economic progress. Intelligent consumption or "rational destruction of utilities" requires "reflection, intelligence and imagination."* Great wealth often breeds great wants, many of which are evil and unwholesome and, like undutiful children, they eventually sink wealth, from which they have sprung, down to poverty. But apart from the economic ruin which extravagant expenditure may bring on the possessors of great wealth, senseless expenditure on such luxuries as do not add anything to the fullness and richness of life is also injurious to the community, because it diverts so much capital and labour from the production of necessities. Nor are the rich alone guilty of harmful extra-

*Cf. "To spend money well is a harder task than to earn money well. In earning the task is generally prescribed, but in spending the spender takes the initiative. It is no longer passive obedience, but a good will that is required." Nicholson : *Principles of Political Economy*, Vol. III. p. 436.

vagance. In most countries the poorest classes are, by reason of their very poverty, the most reckless and extravagant. The opposite vice of niggardliness masquerading as thrift characterises some sections of the people, particularly members of the middle classes, and certain communities like the Marwaris, who often stint themselves and save where they ought to spend freely. It has been observed that "a fuller life in the present for the earner and a greater tendency to leave the succeeding generation, provided that it is well trained and equipped with personal capital, to look to its own welfare, are replacing the older view which inculcated a slow accumulation of savings in order that the children might start with a better equipment of material capital."* This attitude is partly due to a real change in the psychology of the people as one of the many significant results of the War. But it is probably also due to some extent to the great rise in prices and fall in the value of money in recent years. The incomes of the middle classes have not risen in proportion to the rise in prices; and consequently the savings that they may be able to make with economy and self-denial have ceased to appear worth while owing to the reduced purchasing power of money. Indications are not wanting that a similar change, though on a smaller scale, is taking place in India in the attitude of the middle classes whose standard of living has visibly risen during recent times. To some extent, this change ought to be welcome because real thrift often consists not in saving money but in spending it on an increase of well-being in the present so as to make it promote well-being for the future. The unduly timid assiduities of some people as well as the reckless improvidence of others are alike censurable as impairing the economic strength of the nation. It is not possible here to deal in detail with the problem of consumption in India in all its aspects. There is, however, no doubt about the general truth of the contention that the evil of poverty in India, though mainly due to low production, is further aggravated by ill-regulated consumption, and we propose to dwell here more

* W. H. Coates on the Report of the Committee on National Debt and Taxation, *Journal of the Royal Statistical Society*, Vol. XC-Part II, 1927. p. 356.

particularly on one form of unwise consumption which has recently excited much attention. Owing to ignorance as well as the force of custom and tradition large numbers of people in this country (as in others) undermine their physical and hence their economic efficiency by persisting in taking the wrong kind of food and drink, although it is possible to get much more value in terms of welfare from the same income, if a little more attention is devoted to the subject. It is scarcely necessary to point out that there is a vital relation between the physical efficiency of a people and the kind of food which they eat. As the German proverb has it, "Man is what he eats" (Mann ist was er isst). The dietary adopted by people in most of the Provinces in India has so far been controlled by local circumstances and depended on the kind of food that can be grown on the spot. The consequence of this has been that the staple food of the people in some of the Provinces is lacking in important nutrient substances. The differences in the physical efficiency of Indian races such as the Sikhs, the Gurkhas, the Marathas, the Kanarese, the Bengalis and the Madrasis may be chiefly attributed to the difference in their staple diet, and have now been "definitely correlated with differences in the biological value of foods which necessity, habit, or religious prejudice has forced them to use." Lt. Col. R. McCarrison has conducted valuable investigations into malnutrition as a cause of physical inefficiency and ill-health. His researches at Coonoor have shown the relative nutritional values of the national diets in India. Rice, which is the chief food of many people in India, especially in Madras and Bengal, is fundamentally a poor diet deficient in important organic salts, and does not furnish the undefined constituents of food called vitamins, whose importance has been revealed by modern investigations. The wheat and meat-eating people like the Sikhs, Pathans and Gurkhas have a much better physique than the rice-eating Bengalis and Madrasis. The addition of wheat, milk, butter, and meat etc. greatly improves the rice-eater's diet as in the case of the Marathas who take principally millets, such as Jawar and Bajra and sometimes wheat and also milk. The daily use of improper food insidiously undermines the

constitution and this is a matter of far greater importance than is commonly realised. The problem of malnutrition is apart from the problem of poverty, because diet is not simply a matter of securing an adequate quantity of food but of achieving a correct balance of the needful constituents for the maintenance of health and vigour. As the Agricultural Commission point out malnutrition and starvation are not the same. "Actually, a person suffering from malnutrition may be consuming more than his system can utilise, and more than he would normally consume if the diet were properly constituted. Deficiency diseases result from the absence of some essential elements in the diet. Their occurrence is, therefore, no indication of poverty.* and consequent scarcity of food. A dietary conducing to malnutrition may cost more than a well-balanced dietary which promotes health."†

Wide-spread propaganda on the basis of authoritative investigations ought to be useful in enlightening people as to how better value could be got from properly selected food in terms of physical well-being without involving additional expenditure. The "eastern drowsiness" and listlessness which characterise the Indian labour are often largely due to the factor of food, which is not only insufficient but also unbalanced, and it is with the latter aspect that we are just now concerned. About 15 years ago investigations into the jail dietaries of Bengal and the United Provinces were made by Col. McCay which showed that diet is an all-important factor influencing physical development and the general well-being of the people. He considered that the inferior physique and vigour of the Bengali was most probably due to deficiency of protein in his diet, "while the inclusion of wheat in gradually increasing proportions as

*Dr. Slater calls attention to the fact that "in some respects the rise in the standard of living has brought physical disadvantage. Thus for example, rice-mills have multiplied saving house-wives the laborious toil—but perhaps healthful exercise of husking the paddy by pounding—but also robbing the rice of much of its nutritive value, the vitamins in the outermost layer of the grain being removed with the husk by the machinery." Introductory Note to Pillai: *Economic Conditions in India*, p. xiv.

† Report of the Royal Agricultural Commission, pp. 494-495.

one passes north from Bihar and Orissa and the United Provinces to the Punjab, has led to a marked physical change in the population.”§ The improvement in communications and transport ought to help in remedying the deficiencies in the diet of a particular Province by the importation of the requisite food-stuffs from other Provinces. All this, however, assumes a change in the nature of the demand for food-stuffs on the part of the people concerned, and this is a question of education and enlightenment on dietetic matters. Col. MacCarrison’s researches at Coonoor and the publicity which they have received at the hands of the recent Royal Agricultural Commission have aroused considerable interest in the country on the question of evolving a scientific diet suited to the different climatic conditions in the country and the different occupations pursued by the people.† One of the measures suggested by the Agricultural Commission for bringing about an improvement in the general health of the people is the development and conservation of the fish resources of the country—a task in which they invite Government, Local Boards and the rural community in general to participate in an active manner, since the addition of fish offers the best chance of enriching the diet of a primarily rice-eating people.¶ Large sections of the people have no religious or other objections

§ Agric. Comm’s Report, p.493.

† It is of interest to note that at least one political leader in the country has put a revolution in the diet of the people, especially of the Hindus, in the forefront of his programme. Dr. Munje has recently caused great flutter and excitement in the orthodox dovecots by his audacious advocacy of a meat diet for the Hindus. It is unlikely that such a revolution in orthodox ideas and sentiments should take place in the near future. But Dr. Munje’s agitation is symptomatic of the growing attention which is being given to the important question of improving the diet of the people.

¶ See Report, pp. 411-417. The Commissioners also suggest that a Central Institute of Human Nutrition should be established, with which the research, also to be organized by the Provincial Governments, should be co-ordinated. They further recommend a closer collaboration between research on animal nutrition and that on human nutrition and also between all these investigations in India with similar investigations in other parts of the Empire. “The problems are so vast that all the staff and material available should be mobilised to assist in their solution.”

to the consumption of fish and full advantage should be taken of this fact.

Recently the growing habit of tea-drinking has been causing not a little uneasiness to a number of dietetic reformers. The habit is especially prevalent in the Presidency of Bombay. There was a time when it was a fashion on the part of writers and reformers even in England to decry what was called 'the vice of tea-drinking' and declamations against "tea-bibbers" were common.* But the working classes there have persisted in its use in spite of all opposition and declamation until tea has become an important item in their necessities of life. Public opinion with regard to tea-drinking has also taken a right about turn, and tea-sipping instead of being regarded a vice has now come to be a sign of domesticity and temperance. Tea-drinking is generally advocated as a substitute and remedy for drunkenness. Another novel advocacy of tea is to be found in Dr. Slater's '*Some South Indian Villages*' (p. 232), where he remarks that the Indian peasant is very poor in one particular commodity, which he does not properly appreciate, and that is good drink. The great mass of people drink filthy water, water drawn from rivers and irrigation channels and containing every kind of impurity, and from stagnant tanks which are also little better guarded. Dr. Slater believes that "one of the greatest benefits which could be conferred upon India at the present time would be to popularise the use of tea, the cheapest of all boiled water drinks." And he commends the efforts made by the managers of the Buckingham and Carnatic Mills in Madras to popularise tea in the schools, for half-timers and children of mill hands. But the uses of tea as avoiding the dangers of drinking impure water may be regarded as problematic, because these dangers are not eliminated so long as some water at least continues to be used for drinking purposes. The more effective way would be to ensure the supply of pure water. However, as an alternative to alcohol, tea-shops must undoubtedly be regarded as a boon. At the same time there can be no doubt that excessive tea-drinking is harmful to the constitution in a hot climate, especially

* Helen Bosanquet : *The Standard of Life*, p. 310.

when inferior brands are used as in most tea-shops in India. Some steps seem to be necessary in order to ensure that reasonably good tea is sold in these tea-shops instead of the vile decoction generally served, though after all the most effective remedy would be an improvement in the taste of the people themselves. For the rest, we have already admitted that tea-shops have a distinct rôle to perform in the task of checking the growing evil of drunkenness and at the same time providing a harmless stimulant, a need for which in the case of people who have to undergo exhausting physical labour cannot be ignored.

We have touched in a more or less amateurish fashion on one or two problems of consumption with reference to Indian conditions, but for a more adequate understanding of the subject the economist must wait for more light from experts and specialists in other fields.

CHAPTER VI

TRANSPORT

§ 1. Importance of Transport :—Improvements in the means of communication and conveyance of men and goods have always played an important part in the history of civilisation. A good system of communications by land, water, and, we must now-a-days also add, by air, is one of the most important of all the requisites for the prosperity of a nation. It breaks down the isolation of the different parts of a country and brings them into an organic relationship with each other. It increases the contact between town and village to the mutual advantage of both. It is the very life and soul of trade and it acts as a stimulus both to agriculture and to industry. In short, it enables a country to utilise its economic resources to the best possible advantage. The importance of transport from the military, administrative, cultural, and social points of view is hardly in need of special emphasis. Throughout the whole history of India the difficulties of communication have been a predominant factor in determining her political and economic development. These difficulties have been removed, in modern times to a certain extent, by railways, telegraph, motor transport etc. But they still constitute a great obstacle to the advance of modern industry. The expenditure involved in equipping the country with an up-to-date system of transport at all adequate to the requirements of the country would be enormous. India is a sub-continent, the distances to be traversed are enormous and the natural obstacles to be overcome in passing from one region to another are formidable, while even within a restricted area, internal communication often breaks down altogether in the rainy season. Again, India is less fortunate than other countries like England, in respect of waterways, which historically have played a very important part in facilitating commerce in many countries, especially before the advent of railways.

The means of communication in India were comparatively very defective even till as late as the middle of the 19th century,

and were reminiscent of the position in this respect as it existed in England in the middle of the 18th century, though owing to the more favourable climatic conditions the roads were better in India than in England. The railways of course had yet to come and the few trunk roads constructed by the Indian Rulers, especially in Northern India by the Mughals, were thoroughly inadequate even for the very moderate needs of the country in those days.* Many of the so-called roads were mere tracks cut by village carts across the face of the country, and wheeled traffic was for the most part impossible during the rainy season. Pack animals led by *caravans* or *Labans* were the only means of access to many parts of the interior. Moreover, the roads were unsafe being infested by highwaymen such as the Thugs and the Pendharis. There were no navigable canals to speak of, though a few regions such as those along the Ganges and the Indus—which were then great natural highways of commerce—and the coastal districts were more fortunately situated in this respect than others. On the whole, the state of communications in Northern India with its vast plains easily traversable in the dry season, its navigable rivers and a few ‘made’ roads was much more satisfactory than in the Peninsula with its rugged mountainous territory and poor facilities for water transport* except on the two coasts.

We have already discussed the economic and social effects of the imperfect means of communication and dwelt on the isolation

* See Moreland: *India At The Death of Akbar*, pp. 166-67.

¶ “Some idea of the conditions in the South will be gained from the report of the Public Works Commissioners, appointed by the Madras Government. They report that at the beginning of the century (19th), there was an almost complete absence of any roads in the Presidency.....The following description of the best kind of road is very illuminating. They write ‘...nearly the whole of the made roads (so-called) are only so far made as just to be practicable for carts. They admit of carts moving in the dry weather with light loads at a very slow pace and by very short stages. But by far the greater portion of these roads are unbridged and a heavy shower cuts off the communications wherever the stream crosses a line and they are in many cases so unfit to stand the effects of the wheels while the surface is wet, that in monsoon months they are out of use except for cattle or foot passengers.’” Gadgil: *Industrial Evolution of India*, p. 4.

and the self-efficiency of the village and the prevalence of local economy with all its attendant handicaps in respects of markets and division of labour; the immobility of labour and the conservatism of the people; and the violent dislocation of the otherwise smooth routine of economic life in times of scarcity and famine.* A veritable economic and social revolution has, however, been wrought by the modern improvements in communication and transport dating from the time of Lord Dalhousie who initiated a vigorous public works policy. In this chapter we shall give a short account of the various efforts made in this connection and attempt an estimate of their effects, good or bad, indicating the deficiencies and suggesting improvements in the system of communications as it exists today.

We may for the sake of convenient treatment divide the subject into its three main sub-divisions: (I) Railways, (II) Roads, and (III) Waterways.

(I) RAILWAYS.

§ 2. Diversity of relations between the State and the Railways:—A special feature of the Indian Railway System is the diversity of relations between the State and the Railways in respect of ownership and control. Of the important lines situated in British India or in which the Government of India is interested, four are owned and worked by the State (N. W. R., E. B. R., E. I. R., and G. I. P. Railways); six are owned by the State but worked on its behalf by Companies enjoying a guarantee of interest from the Government (B. B. & C. I., M. S. & M., Assam-Bengal, B. N., S. I., and Burma Railways); three important lines (the Bengal and North-Western, Rohilkund and Kumaon and Southern Punjab) and many others of less importance are the property of private Companies, some being worked by the owning Companies, some by the State or by the Companies that work State-owned systems; several minor lines are the property of the District Boards or enjoy a guarantee of interest granted by such Boards. There are also certain Indian State lines like the Nizam's Guaranteed State Railway. Of the 39,048 open route mileage on

* See Chapt. V, Vol. I.

31st March 1927, the State owned 28,004 miles or 71 per cent and directly managed 15,716 miles or about 40 per cent of the total mileage open at the end of the year.

§ 3. Main Periods of Railway History* :—It is necessary to review the history of Indian Railways and the many changes in Government's railway policy in the course of it, in order to understand this perplexing diversity of conditions in regard to the agency by which the railways are managed and of the relations of Government with the various classes of Companies.

Six more or less well-defined periods in the history of Indian Railways may be distinguished: (a) 1844-1869: The Old Guarantee System; (b) 1869-79: State Construction and Management; (c) 1879-1900: The New Guarantee System; (d) 1900-1914: Rapid extension and development and commencement of railway profits; (e) 1914-1921: Break-down of the Railway System under the stress of War conditions; and (f) 1921 onwards: The Acworth Committee and the overhauling of railway policy on the basis of direct management and control by the State.

§ 4. The old Guarantee System (1844-1869) :—The first proposals for the construction of railways were made in 1844 and contemplated the construction of lines by Railway Companies incorporated in England and enjoying a guarantee by the East India Company of a specified return. Accordingly, contracts were made for the construction of two small railway lines near Calcutta and Bombay with the East India Company and the Great Indian Peninsula Railway Company respectively. But the plan of entrusting the construction and management of Indian railways to guaranteed Companies did not come to be generally adopted till after 1854. It was Lord Dalhousie's famous Minute on the subject in 1853, that gave a decisive turn to Government policy in this direction. In the Minute, Lord Dalhousie reviewing the whole situation pointed out the great advantages to India from the construction of a network of railways. He urged the creation of a system of trunk lines con-

* For fuller details regarding the history of Indian Railways see Appendix B to the Report on Indian Railways, 1926-27 pp. 99-103.

necting the interior of each Presidency with its principal port and connecting the different Presidencies with one another. Lord Dalhousie referred in the following terms to the benefits which he expected from railways both to India and England: "Great tracts are teeming with produce they cannot dispose of. Others are scantily bearing what they would carry in abundance if only it could be conveyed whither it is needed. England is calling aloud for the cotton which India does already produce in some degree, and would produce sufficient in quality and plentiful in quantity if only there were provided the fitting means of conveyance for it, from distant plains to the several ports adapted for its shipment. Every increase of facilities for trade has been attended, as we have seen, with an increased demand for articles of European produce in the most distant markets of India. Ships from every part of the world crowd our ports in search of produce which we have or could obtain, in the interior, but which at present we cannot profitably fetch to them, and new markets are opening to us on this side of the globe under circumstances which defy the foresight of the wisest to estimate their probable value or calculate their future extent." He explained his reasons for preferring the agency of companies, under the supervision and control of Government, to direct construction by Government. Not that he had any doubts regarding the capacity of State engineers, but he thought that the withdrawal from other important duties of the large number of officers required, would be detrimental to the public interest, and that the conduct of commercial undertakings did not fall within the proper functions of Government, especially in India, where it was necessary to discourage the people's habit of dependence on the Government for everything which was a serious obstacle to the advance of the country. One of the results which Lord Dalhousie contemplated with satisfaction from rapid railway construction by British Companies was a more extensive employment of English capital and enterprise in Indian trade and manufactures. These companies, he suggested, should enjoy a Government guarantee of interest, for without it private capital would not brave the risks of such pioneer enterprise or undertake expensive engineering work involved in railway construction in a sub-continent like India.

In accordance with Dalhousie's plan contracts were entered into with eight companies between 1854-60 for constructing and managing railways in different parts of India. A fresh stimulus to railway construction was given by the experience during the Mutiny period, when movements of troops and material were seriously impeded owing to defective transport. The main features of the contracts with the early guaranteed companies were as follows:—(i) Free grant of land, (ii) a guaranteed rate of interest, ranging from $4\frac{1}{2}$ to 5 per cent and payable at 22d. per rupee, (iii) utilisation of half the surplus profits earned by the Companies for repaying to Government any sums by which it had been previously called upon to make good the guarantee of interest, the remainder belonging to the shareholders, (iv) reservation of certain powers of supervision and control by Government in practically all matters of importance except the choice of staff, and (v) option to Government to purchase the lines after 25 or 50 years on terms calculated to be the equivalent of the Companies' interests therein.

This system, however, proved to be a great drain on the resources of the State and a burden on the tax-payer in India. The Companies did not earn their 5 per cent until 1900 and called upon Government to make good the deficiency. The deficit in the railway budget amounted to Rs. 166½ lakhs by 1869. This was attributed by several critics like Lord Lawrence, who in his Minute in 1867 had strongly condemned the Guarantee System, to the extravagance of the Companies who had no incentive for economy of construction under the guarantee system.† The Acworth Railway Committee, however, has expressed the opinion that the formation of English domiciled companies was the only wise course for the time in view of the urgent need for railways in India and the shyness of Indian capital making it necessary to offer special attractions to British capital for this purpose.¶ However, others have questioned the wisdom of this policy and denied that English capital could have been attracted only by the inducement of a guaranteed rate of

† See Dutt : *India Under the Victorian Age*, pp. 355-356,

¶ See Acworth Committee's Report, para 188,

profits. For example, it was put in evidence before the Parliamentary Committee of 1872 by William Thornton that unguaranteed capital would have gone into India for the construction of railways, had it not been for the guarantee. England had an immense amount of capital for which there was no scope for remunerative investment at home, and which, therefore, was seeking outlets in South America and other countries, and it was not conceivable that it would persistently have neglected India.* It also remains an unproven assumption that the rate of interest that was actually guaranteed was in point of fact necessary. There are good grounds for believing that British capital and enterprise could have been tapped by the offer of an appreciably lower rate, having regard to the then prevailing easy conditions of borrowing in the English money market. This contention is strengthened by the later experience of Government when they were, without much difficulty, able to enter into contracts under the revised guarantee system on terms much less favourable to the Companies in respect of the guaranteed rate of interest and other concessions. Apart from the loss to the country due to unnecessarily liberal terms granted to the Companies, we may also point out that while Government showed its active interest in the promotion of railways, it did not exert itself to build up any of the industries required to supply the materials demanded by the railways and this made them all the more expensive.

§ 5. State Construction and Management (1869-1879) :— Being dissatisfied with the financial results of the old guarantee system, Government made an unsuccessful attempt in 1862-64 to secure the construction of railways in India on terms more favourable to themselves than those in the contracts with the original Companies. An annual subsidy at a certain rate per mile of line instead of a guarantee was granted to a few Companies like The Indian Branch Railway Company, which later changed its name to Oudh and Rohilkund Company. The Government of India were not prepared to continue the old guarantee system, their objections being the extravagance of the Companies, absence of effective Government control over them, the

* See Dutt : op. cit. p. 394.

inconvenience to Government of a guaranteed rate of interest on the capital of the Companies and the remoteness of the prospect of securing a share of the surplus profits to themselves. Two important changes were consequently made. In the case of some of the more important Railway Companies like the G. I. P. the arrangements regarding the distribution of surplus profits were altered so as to enable Government to claim half the surplus profits for each half-year unconditionally, Government relinquishing its right to purchase the lines at the end of the first 25 years from the dates of the respective contracts. An even more important change in policy—remarkable for the sixties when laissez-faire ideas held the field—occurred when the Secretary of State decided that, so far as capital for new lines in India was concerned, Government should secure for itself the full benefit of its own credit and of the cheaper methods of construction etc. which it was expected it would be able to use. Accordingly for several years after 1869, the capital expenditure was chiefly incurred direct by Government, and no fresh contracts with guaranteed companies were made. It was decided to borrow annually £ 2 millions as the maximum for constructing lines to be managed by the State, and a new cheaper gauge, viz, the metre gauge, was adopted. A vigorous programme of railway construction then followed with satisfactory results so far as the costs were concerned. But the main difficulty was in respect of a continuous and adequate provision of funds. In the first place, the Sind and the Punjab lines (later known as N. W. R.) had to be converted from metre to broad gauge for strategic reasons. In the second place, the financial difficulties of Government were increased by the inroads which the falling Rupee was making on the Government exchequer and also by the famines between 1874 and 1879. These difficulties were aggravated by the Frontier War with Afganistan. Moreover, the Famine Commission of 1880 held that 5,000 additional miles of railway were urgently needed and that the country could not be held safe from famines until the Indian Railway mileage had aggregated to 20,000*. Government was

* By the end of 1879, in about 25 years from the introduction of railways in India, 6,128 miles of railway had been constructed by Companies at an approximate cost of £ 97.87 millions and 2,179 miles by Government at an approximate cost of £ 23.69 millions.

thus forced to the conclusion that the State alone could not find sufficient funds for pushing ahead with railway construction as fast as the Famine Commission recommended, and decided again to take the help of capital borrowed by private Companies, especially because it was then thought that a limit was necessary to the capital borrowed annually by Government,*

§ 6. The New Guarantee System (1879-1900):—Thus by the early eighties the current of thought in favour of State management had spent its main force and a new period in railway history was ushered in, when Government decided again to utilise the agency of guaranteed Companies with certain modifications of the old terms as recommended by the Famine Commission, and contracts were made with the new guaranteed Companies, such as the Bengal Nagpur, and the Madras and Southern Maratha Railway Companies. The chief differentiating features of the new guarantee system were as follows:—(1) The lines constructed by the Companies were declared to be the property of the Secretary of State for India who had the right to determine the contracts at the end of approximately 25 years after their respective dates or at subsequent intervals of 10 years, on repaying at par the capital provided by the Companies. (2) Interest was guaranteed on the capital raised by the Companies at a lower rate, the most usual rate being $3\frac{1}{2}$ per cent. (3) Government retained a much larger share (usually $\frac{3}{5}$ ths) of the surplus profits for its own benefit. Thus the lines constructed under the new system by the Companies were from the beginning the property of Government, though the Companies were given a certain guaranteed rate of interest on the portion of the capital raised by them and were allowed to manage the lines when completed.

Similarly, when the contracts with the old guarantee Companies expired, Government in most cases exercised its right of terminating them, though the method of making use of this right differed in different cases. In some cases, for example, the East Bengal, the Oudh and Rohilkund and the Sind-Punjab Railways, the lines were purchased and transferred to State management.

* Iyer: *Indian Railways*, p. 7.

In other cases like the E. I. R. and the G. I. P. Railways, the lines were acquired by the State, but were handed over again for management to the same Companies under revised contracts. So also, when the contracts with the new guarantee Companies expired, though arrangements were made for the continuance of management by the original Companies, Government secured more favourable financial conditions by various methods, such as reduction in the Companies' share of capital and in the rate of interest guaranteed, and further modification of the clauses relating to the division of surplus profits.

§ 7. The present position :—The existing arrangements between the Government and the Guaranteed Companies may be conveniently summed up at this stage. The State has now come to be the owner of the bulk of the trunk lines. The greater part of the capital has become its property, either through having been originally supplied by it or through the acquisition by the Government of the greater part of the Companies' interests on the termination of the old contracts. The capital originally contributed by the Companies has thus come to be only a small proportion of the total cost of the existing system. When funds are required for further capital expenditure the Government has the option either of themselves providing them or of calling on the Companies to do so. The management of the railways, except in a few cases,* has been left to the Companies, though they are subject to Government control, exercised, since 1905, through the Railway Board created in that year, with regard to matters like the standard of repairs, rolling stock, public safety, coordination of the railway systems, train services, rates and fares, etc. Government have also the power of appointing a Government Director to the Boards of the Companies. All these contracts (except one fixed for a term of 25 years) are terminable at the option of the Secretary of State at specified dates on payment of the Companies' capital at par. The last of these contracts to expire will be the one with the Bengal Nagpur Railway which terminates in 1950.

§ 8. Branch Line Companies :—Other types of railway Com-

* The recent transfer of the G. I. P. and the E. I. R. to State management marks the beginning of a new policy to be described later.

panies also came into existence in this period. Indian States were invited to undertake railway construction in their own territories, and the Hyderabad State was the first to do so extending a guarantee to the N. G. S. Railway formed for the purpose. In this way nearly 5,000 miles have been constructed by Indian States who own the bulk of these lines. An attempt was also made to encourage the construction of feeder lines by Branch Line Companies, who were offered, in 1893, rebates on gross earnings of the traffic interchanged with the main line, so that the dividend might rise to 4 per cent. These rebate terms being found unattractive had to be revised from time to time so as to provide for an absolute guarantee with a share of surplus profits or a more favourable rebate so as to meet the requirements of the market. Under these terms a number of Branch Line Companies were formed. But on the whole, this system has not worked well financially and was adversely criticised by the Acworth Committee who described it as a fifth wheel in the coach. While admitting that it enabled lines to be built which otherwise could not have been built, the Committee recommended that Government should now abandon the old policy by reducing the number of the existing Branch Line Companies by amalgamation and should undertake the construction of such lines themselves except, where they could not or would not provide adequate funds—a contingency which is not likely to arise as things stand.* In conformity with these recommendations Government have decided (1925) to find the necessary capital themselves for the construction of branch and feeder lines. They have also expressed their willingness to construct such lines for purely local or administrative convenience upon a guarantee to the Railway Board against loss, by the Local Government or local authorities concerned. ¶

§ 9. 1900-1914: Rapid Extension and Development of Railways and Commencement of Railway Profits:— The main features of this period were the rapid development of railways as part of a new and much more vigorous policy of national development affecting almost every branch of economic life. The railways attained

* See Acworth Committee's Report, paras, 177-180.

¶ See Report on Indian Railways, 1926-27, Appendix E.

to the dignity of a separate department in 1905, when the Railway Branch of the Public Works Department was abolished, and a Railway Board consisting of a President and two members was established at the head of the railway system under the Department of Commerce and Industry. A fresh impetus was given in 1908 when the Mackay Committee on Railway Finance laid down for the future a standard of £ 12½ millions as the annual programme for capital expenditure on railways, though it was to be subject to periodical revision.* Although Government did not see their way either to attain the standard recommended by the Mackay Committee nor were they allowed to adhere over a series of years to any uniform rate, they spent sums considerably larger than had been the case in previous years. The railway mileage in this period increased from 24,752 in 1900 to 34,656 miles in 1913-14, and the capital outlay from Rs. 329.53 crores to Rs. 495.09 crores.

Another notable characteristic of this period was the commencement of railway profits since 1900. The unprofitable character of railways approximately till that date was due to uneconomical construction and management by the old Guarantee Companies, the construction of unremunerative strategic lines like the North-Western Railway and those constructed for the purpose of famine relief and the absence of traffic to make a success of these new means of transport which could not quite fit in with the existing economic organisation of the country. The losses to the State until 1900 amounted to £ 51.52 millions. After that the Railways began to yield a net return to the State on the capital outlay at charge, thanks to the general economic development of the country and especially of the Punjab and Sind under their irrigation works—which have enabled even the Frontier Railway, for a long time regarded as the cinderella of Indian Railways, to pay its way—and the renewal of the original contracts with the guaranteed companies under terms more favourable to the Government. The gain to the State was small for the first ten years after 1900, but by 1918-19 the total gain had aggregated to £ 44.74 millions. Railway profits, however, are subject to

* See Knowles, *op. cit.*, pp. 340-341.

a remarkable variation from year to year, depending as they do, on the agricultural position and the course of the internal and external trade of the country. The adoption of the recommendations of the Acworth Committee and the retrenchment carried out as suggested by the Inchcape Committee (1922-23) have placed the Indian Railways in a sounder financial position than before. On the capital at charge of the State the gross profits (gross receipts *minus* working expenses) have varied as follows during recent years:—

Year	Percentage	Year	Percentage
1913-14	5.01	1923-24	5.24
1916-17	6.46	1924-25	5.85
1918-19	7.53	1925-26	5.31
1921-22*	2.64	1926-27	5.05
1922-23	4.38		

The Retrenchment Committee laid down that a 5½ per cent net return on the capital outlay should be aimed at by the railways. Regarding the railway profits declared by the Government, Mr. Chandrika Prasad observes, "In declaring surplus profits on the railways, especially during recent years, the ordinary commercial principle of allowing for depreciation on stock has not been applied." He contends that the profits declared must be subjected to considerable discount on this account. This position was upheld by the Acworth Committee which strongly recommended that each railway should make adequate provision annually for the maintenance and the renewal of its permanent way and rolling stock. The question of gross and net railway profits will be further dealt with under Finance.

§ 10. Break-down of the Railway System: (1914-1921):—This period is characterised by the utter break-down and rapid deterioration of the railways, partly because of the strain to which

* In 1921-22, the Railways worked for the first time for many years at an actual net loss to the State, owing mainly to the great stagnation of trade and increase in working expenses.

they were subjected by the necessity of having to provide for the large movements of troops and materials at a time when a part of the rolling stock, staff etc. was required for the construction and working of the military railways in Mesopotamia and other theatres of war, and partly because of the general financial embarrassment of the Government which was compelled seriously to curtail the annual programme of capital expenditure on railways. To add to this all, it was extremely difficult to obtain any railway material from England during this period. Not only had fresh extension of railways to be practically held up but even the existing lines could not be maintained in good condition. The Acworth Committee give in the following terms a picture of the breakdown of the railway system under stress of War conditions: "There are scores of bridges with girders unfit to carry train loads up to modern requirements; there are many miles of rails, hundreds of engines, and thousands of wagons, whose rightful date for renewal is long overpast." It is no matter for surprise, therefore, that loud complaints were made by the public and the trading community regarding the great inconvenience to passenger and goods traffic. Public opinion was becoming steadily hostile to the management of the bulk of the State Railways by English domiciled Companies and demanded that the State should take over the management of its own lines from the Companies.

§ 11. The Acworth Committee and after :—It was also being increasingly realised that the Railway Board, as it was constituted, was not able to take the initiative in laying down railway policy and failed to exercise effective control over the railway administration, especially in regard to fares and rates, being overloaded with routine, trammelled by unnecessary restrictions and handicapped by its ignorance of local conditions and inadequate provision for technical and inspecting staff. So also the need for a fresh lead was felt in respect of the future policy of railway finance. All these questions were, therefore, referred to a special Committee appointed in November 1920, and presided over by a railway expert from England, the late Sir William Acworth. The immediate cause of the appointment of the Committee was, however, the question as to the action to be taken

in connection with the East Indian Railway, a State-owned Railway managed by the East Indian Railway Company, whose contract with Government was terminable in December 1919. As a temporary measure the old contract was extended to the end of 1924, and the general questions arising out of the discussion regarding the respective merits and demerits of various possible systems of management were referred to the Acworth Committee. The Committee after a comprehensive inquiry issued its Report next year embodying its findings on several questions of importance which we now proceed to review. We shall first deal with the State vs. Company management controversy.

§ 12. State vs. Company Management of Railways: General Principles :—The general case for private management of railways may at once be admitted to be very strong.* State management is usually granted to be unobjectionable where the work to be performed is of a routine character, and railways certainly do not answer to this description. This explains why “two-thirds of the railway mileage of the world has been built; two-thirds of the railway capital of the world has been provided; and two-thirds of the current railway work of the world is done by private enterprise; and only the remaining third by State undertakings.”§ Railways are a commercial organisation and the presumption is against bureaucratising commercial organisations. Private management generally means flexibility and enterprise, whereas government management stands for formalism and red-tapeism. Under private management the extension of railway development generally takes place much more quickly than under state management, as a private company plans boldly for the future and is not afraid of taking risks. If a new enterprise seems to offer reasonable prospects of success, and if money is available or can be raised at a reasonable rate of interest the private company goes ahead with it; whereas in the case of the State, owing to the numerous calls on public money and owing to the reluctance of governments to incur unpopularity by

* For a full discussion of this question see Acworth: *State Railway Ownership*.

§ *Ibid.* p. 4.

additional financial burdens, the important work of railway development tends to be neglected. In India, for example, one of the arguments advanced in favour of private company management is that the State has been fitful and parsimonious in the past in its treatment of the Railways. Railroading being a progressive science, new ideas are constantly appearing necessitating the employment of new plans and new methods. This means that much fresh expenditure has to be undertaken from time to time in view of the large profits to be earned in the long run, and the State is generally not in a position quickly to respond to the needs of railway development in the light of new ideas and new inventions.* Another advantage of private management is that, if a company invests unwisely, it is the private individuals who lose their money and not the public. On the other hand, if the State makes improvident investments, the cost of them remains as a permanent burden on the country as a whole. As regards the choice and advancement of the railway-staff, the advantage is clearly on the side of private management. Under the State, appointments to important posts are generally regulated by a literary test and as the result of an examination. This is inevitable, if the evil of political patronage is to be avoided. But such a system of selecting the personnel does not lead to the highest efficiency. Government service also generally means a life tenure except in cases of gross incompetence, and promotion is regulated by seniority rather than by merit or by special qualification. A private company on the other hand, since it must stand or fall by efficient management, has got to be more careful about the manner in which it appoints its officers and grants promotion to them. Real merit is always awarded irrespective of the question of seniority. This makes for the utmost exertion on the part of the officers and other employees who are stimulated by the ambition of rising up to the highest rungs of the ladder in the service. Under State management, there is also a tendency towards lavish expenditure in every respect, as nobody is personally interested in observing strict economy. Private industry, on the other hand, provides a semi-automatic check to this evil as it must care for its shareholders and earn for them the highest possible dividend. Rail-

* See Acworth; *op. cit.* p. 62.

ways are especially unsuited for management by democratic Governments. As Acworth points out, Parliamentary interference generally means running the railways not for the benefit of the people at large but to satisfy local and sectional or even personal interests. Under Parliamentary management it is especially difficult to get the necessary funds for inconspicuous day-to-day improvements which are so important from the standpoint of public benefit, though money may be readily provided if the proposed improvement is more spectacular but really less beneficial.* Another evil, which has been noted especially in connection with State management in France, is that it leads to lack of discipline among the railway staff owing to the operation of political influences. Members of Parliament are inclined to favour the lower staff at the expense of the superior staff because of the greater voting strength of the former. Lastly, the vast patronage in railways has a very dangerous political side under a democratic Government. It has been argued against Company management that during war time it is important that the railways should be under centralised Government control and that Company management is inconvenient from this point of view. The experience of the late War, however, has shown that in the event of a war, it is quite possible to weld together at a short notice the separate railway companies into one homogeneous system, and, therefore, not much importance can be attached to this argument.

§ 13. The case of India :—On theoretical grounds the case against railway management by the State is thus overwhelmingly strong. But when we come to consider, with reference to any particular country, whether it ought to adopt Company or State management, simple appeal to theory is not of much use. If we examine the cases of different countries, we will see that historical causes rather than theoretical considerations have been responsible for any particular system in operation, and that different countries are prospering more or less under different systems. Coming to the case of India, we must remember that here the presumption is in favour of the Continental principle that

* *Ibid*, p. 103.

whatever can be done *by* Government should be thus done rather than the Anglo-Saxon principle, which says that whatever can be done *without* Government should be thus done. Governments undertake railway business for various reasons, such as political reasons, or in order to make up for the lack of private enterprise, or again in order to secure for the people cheaper rates, better facilities and more impartial treatment than is expected under private enterprise. All these reasons have been more or less powerful in India in strengthening the case for State management. Another factor that has to be borne in mind in dealing with the situation in India is that Company management in the true sense of the word is impracticable in this country and, therefore, as the Majority Report of the Acworth Committee points out, the whole reference to foreign countries and the relatively greater success achieved by Company management elsewhere is irrelevant. In India, State ownership already exists for the most part and also direct State management to some extent, as in the case of the North-Western Railway and Eastern Bengal Railway, to which have been added recently, the G. I. P. and the E. I. R. Railways. The major portion of the State-owned railways was, however, managed until lately by Companies with a London domicile, and even today nearly 45 per cent of the State-owned railways are managed by Companies. But the opinion that the management of all the railways should be taken over by the State is gaining almost every moment in strength and vehemence. It has been supported by the Majority Report of the Acworth Committee and non-official Indian public opinion generally. There is a general consensus of opinion that, in any case, management by Companies, at least in the present form, that is to say, by Companies with a London domicile, has got to go. The Acworth Committee, however, were divided as to whether the alternative should be State management, or management by Companies with an Indian domicile. The Majority headed by Sir William Acworth the Chairman, pronounced definitely in favour of the former alternative, for, though they confessed that most of them approached the question with a strong prepossession in favour of private enterprise as a general proposition, the special conditions

in India pointed unmistakeably to State management. *The case for State management in India may be put as follows:—

Though a Company investing its own money, managing its own property and judging its officials by their success in producing results in the shape of dividends, usually conducts business with more enterprise, economy and flexibility than are found by experience to be attained in business directly managed by the State, the English Companies managing State Railways in India have long ago ceased to be Companies in this sense. The property entrusted to their management is not their own and their financial stake in it is comparatively very small. †Such a system has never worked satisfactorily in the past and cannot be made to do so in the future. The management is only nominally entrusted to the Companies, for the Government feeling itself to be the real owner has left really no initiative in the hands of the Company. The Government Director sitting on the Home Board has the power of vetoing any decision of his colleagues. The railway receipts are required to be paid in their entirety into the Government treasury, and money required for revenue expenditure can be drawn only subject to restrictions prescribed by Government and not necessarily to the extent desired by the Company. Creation of appointments etc. are largely controlled by government. Thus, while the Company cannot and does not manage the undertaking, it cannot break new ground in any direction except with the sanction of Government. The Government does not feel an obligation to undertake any initiative itself. Nor can it stir up the Company, if the latter is supine. In short, it is a system under which a progressive Company is hampered by meticulous Government control over every detail of expenditure, and under which, on the other hand, the utmost wisdom on the part of Government

* Cf. Acworth Committee's Report, paras 210-239.

†In this connection, the following figures will be found interesting. The total capital outlay on railways was Rs. 788.67 crores at the end of March 1927. Out of this Rs. 700.96 crores was Capital at charge on State-owned railways inclusive of premia paid in the purchase of Companies' lines. The remainder Rs. 87.71 crores represented Capital raised by the Indian States, Companies and District Boards. By far the greater portion of the capital of State-owned railways, Rs. 661.17 crores, was Government Capital and 1/18th or Rs. 39.78 crores was owned by Companies.

cannot prevent the injury caused by the unwise and unprogressive policy of the Company's Board, both to the revenues of the State and the economic development of the country. As regards the proposal put forward by the Minority that the management should be transferred from English to Indian Companies, the first objection is that the Indian Companies will have only a minority interest in the undertaking. The Government will remain the predominant partner, appoint one-half of the Directors and nominate the Chairman and so retain their control. The division of responsibility between the Government and the Board of Directors will still continue, and the executive officers, with a divided allegiance to a Board of Directors which appoints and pays them, and to the Government which stands behind the Directors, cannot do the best work of which they are capable. Competent businessmen will refuse to join the Board if they find their power limited by Government control and Government regulations, and this seems inevitable under the plan proposed by the Minority. Since it is not proposed that private Companies should buy the railways out and out from Government, as this would involve raising capital amounting to crores of rupees, the financial interest of the Companies, as they are proposed to be constituted by the Minority, is bound to be small. A mere change in the domicile of the Company, therefore, would not improve matters, as Companies substantially independent of Government cannot be formed in India, and without such independence the advantages of private enterprise would not be gained. Indian domiciled Companies, again, would not be able to be of much assistance in raising the necessary funds for railway construction. Government will always have to take the larger share of this work on themselves, and they would find this task much easier under a system of State management than under Company management. Company management whatever the domicile would be unpopular in India, and, if the proposition is accepted that from the financial, economic and political point of view, money required for Indian Railways should henceforward be raised in India itself as far as possible, especially in view of the success of Government in raising large loans in the

country during the war, these loans will be more readily subscribed to by the public, if Government take over the management of the railways themselves. Again, if resort to external loans is necessary, the credit of the Government of India and the Secretary of State as the greatest bankers of the country is an asset of inestimable value. One of the most important arguments in favour of State management in this country is the generally accepted view that Company management has shown itself wilfully negligent of national interests, whether by the manipulation of routes and rates for the benefit of European interests and to the detriment of Indian manufactures and Indian commerce or by refusing a fair field to Indian talent in the railway services, especially in the higher grades. These evils would be obviated under State management. Another advantage expected from State management is the economy in the expenses of working the Railways. At present the State has to pay not only interest on the Company's share of the capital but a share in the profits as well, which under State management would accrue to the Government treasury instead of going to absentee companies in London or to private Companies with an Indian domicile, supposing such were started. There does not seem to be any reason to fear that State management in this country is likely to be less efficient and therefore less profitable than such Company management as can be thought of under the present circumstances. In so far as actual experience of State management in India is any indication at all, it has shown that it does not in any way compare unfavourably with Company management. Nor does there seem to be any truth in the contention that such success as has been achieved by State management in India is due to the existence side by side of railways worked by Companies and to the healthy emulation caused thereby. A serious disadvantage of the present system comes from the fact that the vested interests of the railways in the different parts of the country control not merely the carriage of goods and passengers but also the construction of new lines, trunk or feeder, and the connections of two or more different lines. Spheres of influence have come into existence and form an obstacle in the way of proper railway development. Under State management this evil would be

avoided, and lines will be constructed as demanded by the real interests of the country. Again, under State management, the convenience of traders and passengers would be much better attended to than is the case at present. The Companies have been charged with making the maximum amount of profits their sole object, and there is great dissatisfaction in India on account of their neglect of trade interests and the interests of passengers, more particularly of the third class passengers. The grievances of the public have a much greater chance of being speedily and effectively redressed under State management. The Boards of the Railway Companies situated in London have been generally insensible to such representations from Indian interests as happen to reach them. On the other hand, European merchants being better organised and better represented in England can make their voice easily heard. Such a state of things cannot be regarded as conducive to the rapid development of our commerce and industry. Apart from racial prepossessions, control exercised from a distance of 6000 miles is bound to be highly inconvenient, because it fetters the railway executive on the spot whose discretion is often rigidly circumscribed.

Indian political and commercial opinion is almost without exception united in the demand that State management should be the watchword of railway policy hereafter. Point was lent to this controversy when the contracts with the G. I. P. and E. I. R. were due to expire in 1924-25. In February 1923, the matter came up before the Assembly, which was called upon to consider a proposal put forward by Government to the effect that, while the two Railways should be taken over for management by the State, the door should be left open, after such grouping as might be desirable, for handing over one or both of these Railways to an indigenous Company so as to secure the benefit of Company management. The feeling of Indian non-official members, however, was decidedly in favour of whole-hearted State management, with the consequence that the simple motion for taking the G. I. P. and the E. I. R. under State management was passed, and accordingly these Railways have now been taken over by Government for direct management. The contracts of the various other companies in India

expire at different dates between 1928 and 1950, the last to expire being the contract with the B. N. R., and the probabilities are that all the Railways in course of time will come under Government management, in view of the strength of public opinion and its unmistakeable preference for State management.

§14. Separation of Railway Finance from General Finance:—One of the changes of outstanding importance recently introduced and vitally affecting the efficiency of railways is the separation of Railway Finance from the General Finance. The Acworth Committee urged the adoption of this step on various grounds. In the first place it would remove the element of uncertainty in the annual Budget Estimates due to the inclusion therein of Railway profits. These vary according to the character of the season and trade conditions, with the result that the Estimates might be out by several crores of rupees. The case for separation was seen to be even stronger from the Railway standpoint. The dependence of the Railways on the exigencies of the General Budget and the financial position of the country prevents them from being run on a commercial basis. The arrangement which assumed that the railway concern goes out of business on the 31st of March every year and begins life afresh at the beginning of each official year was obviously detrimental to the railways. The separation of the two budgets was calculated not only to enable the railways to be conducted as a business undertaking but also to free Government from the many difficulties and uncertainties of the old system. In view of the importance of the subject a resolution on it was brought before the Legislative Assembly in September, 1921, when a Joint Committee of the two houses was appointed to investigate the question. The committee declared immediate separation to be outside of practical politics. They were, however, impressed with the necessity of rehabilitating the existing railway lines, which had been utterly neglected during War period, and recommended a guaranteed programme of 150 crores of rupees to be distributed over a period of five years and to be spent upon the improvement and completion of the existing lines, and provision of better amenities for the third class passengers. The Assembly endorsed this recommendation and it was also induced to accept the scheme for

separating railway finances from the General Finances on the condition of ensuring to the latter a definite ascertainable annual contribution from railways, which was to be the first charge on their net receipts. This contribution was settled upon the basis of one per cent on the capital at charge of commercial lines, excluding capital contributed by Companies and Indian States, at the end of the penultimate financial year, plus one-fifth of the surplus profits in that year, interest on capital at charge of strategic lines and loss in working being deducted. The Legislative Assembly stipulated that if, after payment of the contribution so fixed, the amount available for transfer to the Railway Reserve should exceed rupees three crores, one-third of the excess should be paid to the General Revenues. This Railway Reserve is to be used to secure the payment of the annual contribution, to provide, if necessary, for arrears of depreciation and for writing down capital, and to strengthen generally the financial position of the Railways.* The effect of this arrangement upon the finances of the country is that "the Indian tax-payer is now assured of a regular and growing contribution in relief of taxation from his investments in railways; while the task of maintaining a continuous financial policy and of distinguishing between a temporary and permanent surplus or deficit in accounts is immensely facilitated."† The first separate railway budget under this scheme was presented to the Assembly in March 1925. The contribution of the railways to the General Revenue in 1926-27 amounted to Rs. 6.01 crores.

§ 15. Railway Rates Policy:—It has been a long-standing Indian grievance that the railway rates in this country have been based solely on considerations of pecuniary advantage to the Railways and, what is much worse, they have been manipulated so as to help European merchants and hinder the development of Indian industries and enterprise. This complaint was voiced by Sir Ibrahim Rahimtulla in the Imperial Legislative Council in 1915, as also by a number of witnesses before the Industrial and Fiscal Commissions and the Acworth Committee. One

* Report on Indian Railways, 1926-27, Appendix D.

† India in 1926-27, p. 112,

of the specific charges in this connection is that the rates are framed so as to encourage traffic to and from the ports at the expense of internal traffic, thus encouraging the export of raw materials and the import of foreign manufactures.* Indian businessmen and industrialists complain that they have often to pay rates, which they consider unfair, both on the raw materials which they have to obtain from other parts of India and on the manufactured articles which they despatch to various markets. The 'block rates'† system has also aroused much discontent as leading to an artificial diversion of traffic inconvenient to industry and trade. An incidental effect of the railway rates policy in the past has been the congestion of industries in the port towns, which is responsible for many of their present difficulties. For example, the serious labour difficulties are to no small extent due to the concentration of the industries in centres situated far away from the interior. The adverse effect of the railway rates policy on water transport in India is referred to in a later section.

It may be admitted that the determination of railway rates is a very complex process. It is governed by the principle of what the traffic will bear and affected by several factors, such as the competition of water transport, the cost of working particular sections of the line, the convenience and economy of handling large volumes of goods etc. It may also be conceded that Government have always exercised some control over the making of railway rates by fixing the maxima and minima and laying down a general classification of goods, and that the Railways themselves have given certain concessions to Indian industries, such as those in respect of low freight charges on coal. Attention may be invited in this connection to the circular issued by the Railway Board to the

* See Fiscal Commission's Report, para 127.

† Block rates mean higher mileage charges for short lengths imposed on traffic moving from a station, near a junction with another system, towards the junction in order to travel a much longer distance over that other system, with the object of retaining traffic on the line on which it originates and preventing or 'blocking' it from passing off, after only a short lead, on to a rival route.

Railways in 1915 urging upon them the expediency of a favourable treatment of indigenous industries. But as the Fiscal Commission admit, the complaints regarding the unfair treatment meted out to Indian industries were not entirely without foundation. In practice the Railways have enjoyed full discretion in manipulating the rates within the limits sanctioned by the Railway Board and of putting particular commodities into particular classes.* The Industrial Commission after carefully going into the question made recommendations in favour of the rating of the internal traffic as nearly as possible on a basis of equality with traffic of the same class and over similar distances to and from the ports, so as to encourage the transformation of the raw materials into the most finished state possible before export. They also recommended that consignments travelling over more than one line should be charged a single sum based on the total distance.§ The Fiscal Commission endorsed these recommendations and held that within the limitations laid down by their predecessors, special rates should be granted for a term of years to new industries, and even to others if they can make out a proper case for special treatment.† The Agricultural Commission, who examined the question of railway rates policy in its bearing on agricultural development, suggested a closer coordination between the Agricultural Departments and Railways, and recommended the grant of concession rates on the transport of fertilisers, fuel, fodder, milch cattle etc. They further suggested a re-examination of rates on raw material for, and transport of, agricultural machinery and implements.¶

The Acworth Committee reporting on the desirability or otherwise of the present system of control by Government of

* Prof. K. T. Shah holds that "being originally very costly in construction, and still more costly in operation, (and owing) to their being constructed and maintained without reference to the economic conditions of India, the Railway Rates have been fixed without regard to the nature of the traffic and its effects upon Indian Trade and Industry." See Shah : *Trade, Tariff and Transport In india*, p. 397.

§ See Industrial Commission's Report : Chap. xix.

† See Fiscal Commission's Report, Para 12.8

¶ See Agricultural Commission's Report, pp. 377-379.

rates and fares and the machinery for deciding disputes between railways and traders, recommended the establishment of a Rates Tribunal to adjudicate upon disputes between the railways and the public in the matter of rates and fares levied by the former.* After prolonged consideration and consultation with the Secretary of State it was at last decided to set up a Rates Advisory Committee consisting of a President, one member representing the commercial interests and one member representing the Railways. The Committee was accordingly appointed with Sir Narsinha Sharma, lately Law Member, as its first President, with effect from the 1st of April 1926, to investigate and make recommendations to Government on subjects, such as complaints of undue preference, complaints that rates are unreasonable in themselves, complaints or disputes in respect of terminals, and complaints that Railway Companies do not fulfil their obligations to provide reasonable facilities to trade.† The Rates Committee is at present engaged in disposing of several complaints received from the trading and industrial community. Though the Committee's constitutional position is that only of an advisory body, whose findings may or may not be accepted by the Government of India, the latter will not find it easy consistently to disregard its decisions.

§ 15. Reorganisation of the Railway Board:—We have already discussed the defects and shortcomings of the old Railway Board. The Acworth Committee suggested a reorganisation of the Board so as to make it a thoroughly capable agency through which the Government of India could exercise an effective supervision over the whole railway system in the country. The Railway Board as now constituted consists of a Chief Commissioner, a Financial Commissioner and two members. Instead of the Acworth Committee's recommendation of three Territorial Divisions with a Commissioner in charge of each, the plan of dividing the work on the basis of subjects has been adopted. One member deals with technical subjects, and the other with general administration, personnel and traffic subjects, the Financial

* Acworth Committee's Report, para 156.

† Railway Report 1926-27, para 12.

Commissioner representing the Finance Department on the Board and dealing with all financial questions. The Board is assisted by five Directors for Civil Engineering, Mechanical Engineering, Traffic, Finance and Establishment, who relieve the Chief Commissioner and the members of much current work thus enabling them to devote their attention to larger questions of railway policy, to tour over the various railway systems and to maintain personal touch with Local Governments to a greater extent than was previously possible.

Government, however, did not accept the Acworth Committee's recommendation that the Railway Board should be placed under a Member of Council in charge of a new Department of Communications responsible for Railways, Ports, and Inland Navigation, Road Transport, and Post and Telegraph. The position of the Board as a department of the Government of India has thus been maintained under the Member for Commerce and Railways.*

§ 16. Railway Advisory Committees:—The Committee recommend the establishment of Central and Local Advisory Councils to give the Indian public a voice in railway management. Accordingly all State-owned Railways now possess Advisory Committees. There is also a Committee of the Central Legislature consisting of representatives from the Assembly and the Council of State.

§ 17. Indianisation:—Both the Acworth Committee and the Lee Commission (1923) recommended the extension of facilities for training Indians for the superior Railway services, a standard of 75 per cent of such posts being laid down by the latter body. Government have accepted this recommendation and accordingly the Railway Board have already taken steps to extend training facilities, which are an essential preliminary to the Indianisation of the railway services. A Railway Transportation School has already been opened at Chandausi for the training of subordinate officers, and some Area Schools have been started for the training of railway staff. It has also been decided to establish a Staff College for the training of Railway Officers at Dehra Dun.

* Report on Indian Railways, 1926-27 Appendix, C.

The Acworth Committee made certain recommendations in connection with the meeting of popular grievances. Government have already taken certain steps, such as additions to the rolling stock, extension of platform and waiting room accommodation, erection of new stations, provision of water supply, appointment of Controlling Passenger Superintendents etc. This is as it should be, considering that the third-class passenger contributes the largest amount to the railway earnings from passenger traffic; and the good work already started deserves to be further extended.

§ 18. Economic effects of railways :—The advantages of railways from the national, social and cultural point of view are obvious and need not be dwelt upon here. Efficient administration as well as military defence, internal and external, also require a properly developed system of railway communications. The economic effects of railways are most important. Famine relief in a country like India necessarily depends on an efficient railway system for a quick conveyance of food-stuffs to the affected area. It may further be claimed for railways that they give a powerful impetus to the general economic advance of a people making them more and more capable of resisting the effects of a drought. They also bring about an equalisation of prices throughout the country as well as their conformity with world prices. Railways further create new employment and make possible a more even distribution of the population. They are an essential adjunct to the internal and external trade of the country and the following figures show the close connection between the growth of trade in this country* and that of railway transport.

Year	No. of miles open for traffic	Passenger traffic	Goods traffic
		Total No. of passengers (In thousands)	Total No. of tons (In thousands)
1893	14,465		28,847
1898	21,993	151,566	35,642
1908	30,576	321,169	62,398
1913-14	34,656	457,718	82,613
1926-27	39,048	604,371	85,833

* See Kale : op. cit. Vol. I, p. 319; also Railway Report, 1926-27.

The rapid industrialisation of India largely hinges on a satisfactory railway development, facilitating the transport of coal and raw materials as well as the distribution of finished goods. Railways also stimulate engineering industries, and are intimately connected with the progress of telegraphic and postal communications. The effect of railways on the forests has been on the whole beneficial. Railway transport facilities and the demand for railway sleepers have greatly stimulated timber growing. It may also be remarked that in an indirect way railway construction has forcibly attracted the attention of Government to the importance of forest conservation. For it was seen that, without the institution of a proper machinery for ensuring the conservation of forests, there was a great danger of their being recklessly destroyed for the fuel required by the railways. The growth of towns and port development are also rendered possible by railways. The invaluable assistance which railways can render in conducting various publicity campaigns for the improvement of sanitation as well as for the introduction of reform in agricultural practice has already been incidentally referred to.* Lastly, government revenues benefit both directly and indirectly from the railways, directly because Government share in the profits from the railways, and indirectly, because they increase the total wealth of the country and consequently the taxable capacity of the people.

Railways, however, have not been an unmixed boon in India. We have already spoken about the part which railway construction has played in this country in hastening the destruction of the indigenous industries and in bringing about the one-sided economic development of the country, under which its exports consist almost entirely of raw materials and its imports almost entirely of manufactured articles. As regards the help derived from railways in the matter of organising an effective famine relief, we must not ignore that there is also another side to the picture. Railways have increased the ruralisation of the country by contributing to the decline of the indigenous industries and this has rendered a large number of people, especially artisans like weavers, more susceptible to famine than they used to be.

* See Vol. I p. 277.

Thus if railways have facilitated the work of famine relief, they may be said, on the other hand, to have increased the volume of this work. It has also been urged that the argument about the equalisation of prices cuts both ways. It shows that the whole of India has become one market for the goods produced in the country, which is undoubtedly a gain. Outright starvation owing to local failure of crops has been rendered practically impossible. On the other hand, however, from the consumer's point of view it may be urged that particular localities fail to reap the full advantage from occasional bumper crops and low prices. Railway development in this country has also meant the introduction of foreign capital and foreign investment, and this, as we have already seen, has brought certain disadvantages along with some advantages.

§ 19. Need for Further Railway Department:- All the adverse effects, however, are properly attributed not to railway construction as such but to the manner in which it was brought about and the undue haste that was displayed in connection with it. We must not, therefore, be led by some of the unfortunate effects that have actually followed from railway construction in India to suppose that it would be in the interests of the country to impede further railway development. On the contrary, it is of the greatest importance that, subject to proper safeguards, railway development should be pushed as fast as possible, in order to expedite the industrial and commercial progress of the country. As already the Famine Commission of 1880 expressed the view that about 20,000 miles of railway were essential for the safety of this country in respect of famines. This limit has already been exceeded and, in 1926-27, the total railway mileage open for traffic stood at 39,049. And yet it is generally held that from the point of view of the total requirements of the country, a very considerable further increase is essential. The Mackay Committee of 1908 said "Even an estimate of a 100 thousand miles of railway...was short of what would ultimately be found necessary in India and that there were fruitful fields for large reproductive expenditure on railways in the country for many years to come, the only effective limit on the amount to be spent in any year being for many years the

amount that could be provided.”* That India is poorly provided with railways can be seen from the fact that, while Europe (excluding Russia) covers 754,000 miles and has 190,000 miles of railways, India contains 1,803,000 miles of country and has but 39,712 miles of railway.§ The following figures are of interest in this connection.

MILEAGE OPEN.

Per 1,000 square miles of territory.		Per 100,000 of the population.
Belgium	396	62
United Kingdom	195	50
United States	70	224
Japan	32	15
India	20	11

Whether we judge India by the standard of territory or of population, it will be seen that she is much worse provided than many other countries with railway facilities. It would of course be absurd to contrast the railway mileage of agricultural India with its vast mountain ranges, great river estuaries and wide-spreading deserts and barren places, with that of highly industrialised, compact countries like England whose every square mile, almost, is made to contribute something to the national income. Further it must be remembered that the need for communications in India can most effectively and cheaply be met in many cases by mechanised road transport and water carriage in preference to railways. But even after allowing for all this, there is undoubtedly a great deal of work which still remains to be done by way of extension of railways. Government have realised this fact and have laid down a large programme for the next five years, at the end of which an addition of 6000 miles of open lines is expected and another 3000 miles will be under construction.† It is proposed to make a fresh addition of approximately

* See K. V. Iyer: *Indian Railways*, p. 28.

§ Speech of the President, Indian Railway Conference, 1918.

† See Agricultural Commission's Report, para 311.

1000 miles every year for some time to come. The special features of this programme are intimate consultations with Provincial Governments with regard to local needs, absence of ambitious projects of trunk lines with which India is already on the whole well served, concentration on branch and feeder lines intended to fill in the interstices of the network of trunk lines, so that the benefits of railway service may be brought right to the doors of the rural population. * This programme may be approved of provided alternative methods of transport are also properly attended to and the relative advantages between railway construction and other forms of transport are in every case properly weighed and considered. It is also important that every possible effort should be made to raise the required capital in India if only to keep within bounds the further growth of foreign capital in the country. Lastly, it is essential that railway industries should be developed and fostered along with railway construction. This is a matter which has so far been almost entirely neglected. The danger of India's dependence on outside supplies for railway materials even for ordinary repairs was fully disclosed in the late War. It is urged, therefore, that steps should be taken to put an end to this dependence. Otherwise also, in the general interests of industrialisation, the case for Railway Industries is clear.

(II) ROAD TRANSPORT.

§ 20. Recent History :--The unsatisfactory state of road transport in India about the middle of the last century has already been alluded to. The East India Company being mainly a commercial corporation neglected an important duty of a civilised government since it took little interest in road making. The limited progress that was made was due to the initiative taken by individual administrators like Lord William Bentinck, who revived the idea of a highway connecting the North of India with Bengal, which resulted in the construction of the Grand Trunk Road linking Peshawar with Delhi and Calcutta. The little importance attached by the Company to the road needs of the civil population is shown by the fact that roads were then placed in

* India in 1916-17 pp. 163-166.

charge of Provincial Military Boards instead of being entrusted to a special Public Works Department.

India, however, entered upon a new epoch of road-making during the time of Lord Dalhousie, who, in addition to his active interest in the promotion of railways, also initiated a more vigorous road policy, and for this purpose there were created, over and above the central Public Works Department, similar Departments in each province in 1855 replacing the old Military Boards. A second factor which has promoted road development during the last seventy years has been the influence of railways. As railway construction proceeded apace it became increasingly necessary to build roads to feed the railways rather than to compete with them, "leading to a demand, which remains today far from being completely satisfied, for bridged and metalled roads which would give access to the railways at all times of the year."* It is necessary, however, to point out that the extension of railways and the intimate financial interest of the Government in their profitable working have led to a certain neglect of roads.† The progressive policy of Lord Mayo and Lord Ripon with regard to Local Self-Government, under which local control over local affairs was provided, acted to some extent as a stimulus to road development. The total effect of all these factors is reflected in a considerable activity in road-building during the last seventy years or so. "The Grand Trunk Road has been extended from the Ganges Valley to Peshawar, good metalled arterial and district roads have been driven over the plains and through the hill of every part of India, and thousands of miles of serviceable 'Kacha' or non-metalled roads and useful bridle-tracks have been made. There can be no question that every district in India has immensely increased the amount of wheeled transport within its limits, even during the past two or three decades, and the extent of this expansion is a measure of the growth of India's road-system and of its economic value to her people."§ This activity, however, needs to be speeded up, for

* Agricultural Commission's Report, p. 370.

† Shah, op. cit.

§ India in 1926-20, p. 267.

the road making activity so far has only resulted in giving India a total mileage of less than 2,20,000 of metalled and unmetalled roads, which, considering the continental dimensions of the country, must be regarded as meagre. The following figures show that India suffers by comparison with other progressive countries in this respect.

	Nine Major Provinces of India		United State	
Density of population per square mile	240		31.5	
	Per 100 sq. miles of area	Per 100,000 of population	Per 100sq. miles of area	Per 100,000 of population
Mileage of all roads	20.18	84	80.00	2,500
Surfaced roads	5.38	22	12.05	383
Percentage of roads surfaced	26.5		15.0	

This comparison is specially relevant as both India and the United States are characterised by their large extent and predominantly agricultural population. This deficiency of roads is keenly felt in rural areas in respect of smaller feeder roads connecting with trunk roads or the railway line, and many a village continues to be inaccessible and is denied facilities of communication.

Apart from the inadequate equipment of the country in the matter of roads, another unsatisfactory feature is the fact that existing roads have been allowed to deteriorate in recent years. This deterioration has been most marked in the case of roads maintained by Local Bodies. Their poor resources coupled with the increased cost of labour and materials have been responsible for this state of affairs. We must, however, reckon with a new factor in the situation, viz., the astonishing rapidity with which

* Agriculture Commission's Report, para 219.

motor traffic in the shape of the private car and the public motor omnibus has sprung up all over India in recent years, thus creating an entirely new range of problems of road construction and maintenance. Indeed the motor lorry has scarcely made an impression on the bullock-cart as regards conveyance of agricultural produce and manufactured articles even for long distances, owing, *inter alia*, to the difficulties presented by the hopeless condition of many roads and the presence of many unbridged rivers even on the arterial roads. But as these difficulties are overcome, we may expect a considerable part of the goods traffic to be captured by mechanised transport, especially in view of the improvements that are taking place in the technique of the trucks.

§ 21. Need for more Roads:—We need hardly stress the importance of good road communications in a continental country with predominant agricultural interests and with its industries struggling to develop. As the Agricultural Commission remark, "Transportation is an integral part of marketing, and modern commercial development tends everywhere to enhance the value and importance of good road communication." India has a large volume of internal and external trade which requires to be handled from year to year. The external trade of the country exceeds an annual average of Rs. 600 crores, and though no satisfactory statistics are available regarding internal trade, it is undoubtedly of much greater volume than the foreign trade of the country. These branches of trade are moreover capable of considerable expansion in the near future. Also, the provision of good communications is the surest way of stimulating agricultural production and raising the standard of life in rural areas. In speaking about the railway rates we have referred to the desirability of effecting the decentralisation of industries whose present concentration is a source of many of their difficulties, especially in connection with the labour supply and housing. Again, roads will be of particular assistance for the development of industries connected with the preparation of agricultural produce for export or internal consumption. They will also facilitate the establishment of "garden factories" and thus evolve a form of industrialism most suited to the needs of

the Indian worker who thrives best in a rural environment. The example of foreign countries should serve both as an encouragement and a warning. The United States and Denmark owe not a little of their prosperity to their excellent system of communications and mechanised transport. On the other hand, the blighting influence of poor communications is illustrated by Russia, which in spite of her great agricultural resources has been at times scarcely able to feed the population in her towns and industrial areas, while the wheat has been rotting in her rich southern fields.* Lastly, the large forest wealth of India can only be exploited properly with the help of suitable road transport.

§ 22. Roads vs. Railways:—Though a considerable expansion of railways has been planned for the near future, it is hardly likely that for many years to come this vast country will be provided adequately with railways as judged by its needs and the standards attained in some of the foreign countries already alluded to. For opening up the hinterland and linking it with the large industrial centres and ports, reliance will have to be placed to a very great extent on roads. A network of arterial and feeder roads is what the country requires. No doubt the construction of roads involves heavy initial expenditure and further expenditure for maintenance and repairs from year to year. The railways are, however, an even more costly form of inland transport, at any rate, for local traffic. As Prof. Shah points out, "the capital outlay on roads good enough to permit of regular motor transport, would no doubt be very considerable: though nowhere near the £ 10,000 or more per mile which the rail road has cost."*† There is, however, no real opposition between railways and roads; both are wanted in proper proportions and both have their appointed place in the economy of the country. For relatively lighter traffic and for short distances the road is probably more suitable, especially as it can be constructed almost anywhere at a considerably lower cost than a railway. At the same time it must be remembered that conditions

* cf. Colaco: 'The effect of Improvements of Roads on Education and Agriculture.

† Shah : op. cit. p. 400.

of weather in India, alternating between extreme dryness for many months of the year and continuous and heavy rain-fall concentrated in a short period, are likely to render the maintenance of roads capable of carrying heavy motor traffic extremely expensive, and the advantage here would probably be on the side of railways. Generally speaking, however, road transport will be cheaper than railway transport, as it does not require stations, sheds, signals, sidings, etc., nor does it involve any loss of time at the termini with their special charges, or problems of carrying half-empty wagons, and of allowing a good deal of rolling stock to remain idle etc.* It, has however, been pointed out that the cheapness of road transport is in some measure due to the fact that the heavy cost of maintaining roads suitable for mechanised transport has to be borne at present mostly by the general tax-payer, while the railways have to pay for the whole cost and upkeep of their permanent way. But even supposing that the idea, at present under contemplation, of making the motor traffic bear at least a part of the charge of maintaining the road-way is put into effect, road transport will retain the advantage of greater cheapness. This applies, as already stated, to lighter traffic and short journeys. On the other hand, the railways will hold their own and will be a more convenient and economical form of transport for heavy loads and longer distances, owing, among other things, to their much smaller running charges. The point that there is no real opposition between the two forms of transport has been well put thus, "The road system links up the cultivator's holding with the local markets and the nearest railway station, while the railway provides the connecting links between the area of production and consumers at a distance, and between the manufacturer in the town and the cultivator who purchases his ploughs, his fertilisers, or his cloth. Without good roads and sufficient roads, no railway can collect for transport enough produce to render its operations possible, while the best of roads cannot place the producer of crops in touch with the consumer."† There is therefore no reason to suppose that

* Shah : op. cit. pp. 403.

† Agricultural Commission's Report, para 312.

the national investment of some Rs. 700 crores in railways is likely to be jeopardised by the extension of road communications. No doubt, a certain amount of competition between railways and roads cannot be avoided, and the railways in India are beginning to feel the pressure of this competition not only in the neighbourhood of large cities and suburbs but also in other parts of the country, where motor services parallel or short-circuit railway routes, as between Poona and Ahmednagar. The general policy adopted by the Railway Administration is to afford to the public an equal or better service than road transport can give, while taking full advantage of the additional business brought to railways by such motor transport as can act as feeder or distributor. Among the methods of meeting road competition are railway omnibus services such, for example, as those run by the E. I. R., and also self-propelled coaches like the sentinel services and shuttle trains.* It may thus be difficult to arrange for a policy of coordination between the two forms of transport. It is possible, however, in future while planning new programmes of road and railway extension to adjust them in such a way that roads may be designed to serve rather as feeders of the railways than as competitors for such traffic as the railway is capable of handling more efficiently and economically. We, therefore, fully endorse the view of the Agricultural Commissioners that it may be found possible in the future to avoid in India the senseless and wasteful competition between rail and motor traffic, that is today taking place in many European Countries.*

§ 23. Recent Developments:—The rapid extension of motor traffic in India in recent years has led to a growing realisation on the part of the Imperial and the Provincial Governments of the necessity of a comprehensive road programme. Road Boards have already been established in Bombay, Burma, Madras, the Punjab, and the United Provinces. The function of these Boards are mainly advisory except in the Punjab and Burma, where they are also entrusted with the distribution of grants-in-aid from provincial funds. Even greater significance attaches to the appointment by the Government of India,

§ Railway Report, 1926-27, p. 47.

in November 1927, of the Road Development Committee consisting of fourteen members of the Central Legislature and presided over by Mr. M. R. Jayakar of Bombay. The Committee was asked to make recommendations on (1) the desirability of developing the road system of India, (2) the means by which such development could most suitably be financed and (3) on the coordination of road development and research and road construction by the formation of a Central Road Board with due regard to the distribution of central and provincial functions. The Committee has finished its deliberations and its report is being awaited with considerable interest.

§ 24. Road Finance:—In connection with the question of providing the requisite finance for road development several suggestions have been made. It has been suggested, for example, that a re-classification should be made so as to transfer some of the local roads to the category of arterial roads, in order to reduce the burden on Local Bodies enabling them to devote more attention to feeder roads and roads of purely local importance. The Local Bodies also require more liberal financial assistance from provincial funds. The Agricultural Commission express the view that the policy of road development would be much better carried out if, instead of relying solely on current revenue, loans were raised for financing road programmes. They hold that in view of the quasi-permanent character of the roads and the works connected with them the annual amount required for the amortisation of provincial loans raised for this purpose should not be a heavy charge on the resources of a province for the upkeep of local village roads. They recommend the revival of the old system of corporate labour of the village community which may receive financial assistance from Government, provided it is prepared to do its part of the job.*

It is understood, that the Road Development Committee has recommended the levy of a development tax by the Central Government of two annas on every gallon of petrol produced or consumed in India for financing its scheme of road development, having

* Agricultural Commission Report, paras. 306-307.

regard to the increasing use of roads made by the motor traffic subjecting them to heavy wear and tear.*

(III) WATER TRANSPORT.

§ 25. The Economics of Water Transport:—We have already referred to the important part played by water transport, especially in the carriage of bulky commodities, before the era of railways, and even today it continues to play a by no means negligible part even in inland trade. As regards oceanic transport it has assumed gigantic dimensions in modern times, thanks to the great development in the technique of maritime transport which has brought into existence a huge international traffic in cheap bulky goods. Water transport possesses certain special advantages over road and rail transport. Firstly, except in the case of artificial navigable canals there is no cost of construction and even in the case of navigable canals the cost is much smaller than that of railway construction. The charge of maintaining waterways is also negligible. No doubt, there is a certain capital outlay involved in providing terminal facilities like docks, wharves and warehouses, but this again is moderate as compared to the cost of similar provisions in the case of rail transport. The cost of ships and of motive power similarly compares favourably with the cost of railway engines and rolling stock. Again water transport is more suitable for the carrying of large and bulky cargoes in single units, and the running charges load for load are much cheaper. "It has been estimated that a railway wagon weighs from one-half to three-fourths of the weight it can carry while canal boats weigh only one-fifth or one-sixth of their total carrying capacity." These benefits are intensified in the case of oceanic transport, as the open sea is an international highway open to all for communication. In spite of all these advantages, however,

* It is understood that the Road Development Committee has made the following further recommendations;—(1) Creation of a Standing Committee of the central legislature to deal with roads, (2) and of Provincial and District Road Boards, (3) holding an annual Road Conference to discuss subjects connected with road transport and (4) a reduction of the import duty on parts and accessories of motor cars to 15 per cent *ad valorem*.

water transport has failed to hold its own in regard to inland trade. The reasons usually put forward to account for this are the hostility of railways and their greater speed. English canals which played such an important role in the early days of the Industrial Revolution have been thrust into the background since the advent of railways and the same is more or less the case with regard to inland transport in India today. In some countries, however, like France, Belgium and the United States, inland water transport continues to flourish under the fostering care of the respective governments.

With reference to India the discussion of the subject of water transport may conveniently fall under two broad divisions: (A) Inland waterways and (B) marine transport.

§ 26.(A) Inland Waterways:—India is not favoured by nature to the same extent as England with rivers which serve the purpose of natural waterways. There is, however, a contrast in this respect between the rivers in Northern India and those of the Peninsula. It is stated that there are about 26,000 miles of navigable waterways in connection with the great river systems of Northern India. The Indus, the Ganges, the Brahmaputra, and the Irrawaddy are navigable by steamers all the year round, or for the greater part of the year, for hundreds of miles above their mouths or above the heads of navigable canals traversing their deltas. Thus the Indus is constantly navigable as high as Dera Ismail Khan in the North-West Frontier Province, 800 miles inland. Its tributaries, the Chenab and the Sutlej are open to small craft all the year round. The Fuleli Canal and the Eastern Nara may be regarded as navigable branches of the Indus. The Ganges is navigable as high as Cawnpore and steamers also pass up the Gogra as far as Fyzabad. The development of rail traffic has, however, led to a considerable decline in the steam navigation on the Indus and the Upper Ganges. The Brahmaputra is navigable by steamers as high as Dibrugarh and there is steam navigation on its tributary, the Surma, as far inland as Sylhet and Cachar. The Hooghly is navigable all the year round up to Nadia and fur-

* See. Shah, op. cit. pp. 405-408.

† See Vo. I, P. 12 and 14.

ther up from July to October. Burma has the greatest facilities for inland navigation which is extensively practised in that province. Apart from the Naya and Kaladen river in the Arakan Division and many others falling into the Bay of Bengal, the largest of these rivers, the Irrawaddy, which traverses nearly the whole length of Upper and Lower Burma, is navigable by steamers all the year round for more than 500 miles from its mouth, while steam launches and country boats can proceed much higher. The numerous deltaic channels of the Irrawaddy and its tributaries are also navigable to some extent.

The rivers in the Peninsula do not, however, lend themselves to navigation. According to season they either flow in torrents or are reduced to mere strings of pools amidst a wilderness of sand or deep gorges, making navigation impracticable. The rocky beds and swift floods of some of the rivers like the Narbada and Tapti are insuperable obstacles to navigation. The Mahanadi, the Godavari and the Krishna are indeed navigable in their upper reaches but the traffic on them is not very considerable.

In addition to these somewhat restricted facilities for river traffic in the country, there are all round the coast innumerable small rivers, creeks and backwaters affording facilities for water transport which are fully utilised by small native crafts; but outside the zone of such operations inland navigation is practically confined to the deltas and valleys of the great rivers which form the natural waterways of the country.*

Inland navigation was largely resorted to in the old days and there was a considerable volume of river traffic in the time of the Mauryan and the Moghul Empires. For example, the Ganges was the great natural highway of commerce, and on its banks flourished several towns like Mirzapore which was a great centre of trade with Central India and Bengal. Since the advent of railways, however, inland navigation has received a set-back. As the Industrial Commission point out, "In the absence of a representative specially charged with their

* Indian Year Book, 1925, pp. 229-230.

interests (that is, those of the existing waterways) the vested interests of the railways have prevented waterways in India from receiving the attention that has been given to them in other countries with such satisfactory results."* The Acworth Committee also repeat the view that waterways have suffered by unfair competition on the part of railways, and they cite the case of the river port of Broach in Bombay and the Buckingham Canal in Madras in support of their contention.

At one time there was a good deal of agitation in favour of navigable canals.† Sir Arthur Cotton, "the architect of the magnificent Kaveri and Godavari works," prepared an ambitious scheme of navigable canals which was put before a Parliamentary Committee in 1872. He made out a strong case for water-carriage facilities, which he thought were more suitable for India and less expensive than railways—which then seemed to have failed miserably—and had the further advantage that they could be combined with irrigation. "The principal lines of navigation which Sir Arthur Cotton recommended were (i) from Calcutta to Karachi up the Ganges and down the Indus; (ii) from Coconada to Surat up the Godavari and down the Tapti; (iii) a line up the Tumbhadra to Karwar on the Arabian Sea; and (iv) a line up Ponang, by Palaghat and Coimbatore." He estimated that a capital outlay of not more than £ 30 million all told would be required to construct all the necessary navigable canals. The scheme was suffered to drop, however, because of the heavy expenditure it entailed, and even more because it was difficult for Englishmen to understand the value of canals, in India as experience in their own country seemed to decide the case in favour of railways. The opposition on the part of the railways in India was also another factor which counted.

The construction of navigable canals, either in conjunction with irrigation or for transport pure and simple, did indeed appear particularly attractive for a time as the railways were a losing concern till the close of the last century. Much of the enthusiasm for it, however, was lost

* Industrial Commission's Report, para 279.

† See Dutt : *India in the Victorian Age*, pp. 360-377.

with a turn in the tide and the commencement of railway profits since the beginning of the present century. There are only a few navigable canals today such as the Ganges Canal from Hardwar to Cawnpore and the Buckingham Canal parallel to the East Coast in Madras. The numerous irrigation canals already referred to are for the most part not suitable as waterways. The two types of canals cannot often well be combined together. Generally speaking, navigation cannot be maintained during the season of short supply of water except to the detriment of irrigation. Irrigation canals are moreover usually shallow and circuitous in their course and pass through sparsely populated rural regions to serve the needs of cultivation. Canals for navigation must, on the other hand, pass through industrial and commercial centres in order to attract sufficient volume of business. Conditions are, however, more favourable in the deltaic tracts of Bengal, Orissa, Sind and Madras. In Eastern Bengal particularly there is considerable scope for connecting the canals to improve the navigation facilities in connection with its great river system.

In spite of the physical limitations imposed upon inland navigation in India there still appears to be some scope for improvement in the existing waterways. The Industrial Commission recommend that the Government of India should take up the question and see to it that the railway and waterway administrations worked together harmoniously for those parts of the country which are served by both and that the proposal of forming a Waterways Trust should receive the careful consideration of Government. (Para 279.) Inland waterways, properly developed, would relieve the existing congestion of the railway system and serve the needs of small-scale transport in the country. It may also be possible to adapt at least some of the irrigation canals to the needs of navigation.

§ 27. (B) Marine Transport:—As regards external water transport, although India does not possess the advantages of England with her indented coast-line and natural harbours, she occupies a maritime position of considerable importance. As Mr. Haji remarks, " A country set like a pendant among the vast continents of the Old World, with a coast line of over 4000 miles and with a productiveness of numerous articles of great

use, unsurpassed elsewhere, is by nature meant to be a sea-faring country. Her ports are adequate in size and numbers to meet the various requirements of her products. **

Perhaps the picture is drawn here in excessively bright colours and does not give sufficient weight to India's deficiency of natural harbours. At the same time, as already pointed out, she may well aspire to become one of the principal carriers of the world on account of her extensive sea-board and her favourable position in respect of the rest of the world. Till about the beginning of the 19th century, India could be spoken of as a great sea-faring country. "Ship building was in so excellent a condition in India that ships could be (and were) built which sailed to the Thames in company with British-built ships and under the convoy of British frigates. The Governor-General in 1800, reporting to his masters in Leadenhall Street, London, said: 'The Port of Calcutta contains about 10,000 tons of shipping, built in India, of a description calculated for the conveyance of cargoes to England. 'The teak-wood vessels of Bombay were greatly superior to the 'oaken' walls of old England.'†

Speaking of the period at the death of Akabar Moreland points out that the great bulk of the commerce in the Indian seas was carried in ships built in India and that India had also great passenger ships much larger than any in contemporary Europe with the exception of the ships built by the Portuguese §

The introduction of iron-built ships, however, deprived India of her differential advantage in respect of her large supplies of excellent timber. The rapid improvement in naval architecture and the introduction of mechanised sea transport, together with the jealousy of the English shipping interests and the operation of the English Navigation Acts which were applied to India as she came more and more under British control, may be

* See S. N. Haji : *Economics of Shipping*, pp. 365-366.

† See Digby: *Prosperous British India*, pp. 85-86.

§ Prof. Radhakumud Mookerji in his *History of Indian Shipping and Maritime Activity* talks of "the long and brilliant career lasting over 20 centuries" of the Indian shipping and ship-building industries.

regarded as the chief causes which led to the decay of Indian shipping.*

§ 28. The difficulties of Indian enterprise in shipping:—We may now proceed to indicate the position held by Indians in the coastwise and the oceanic trade of India. The total value of our coastal trade in 1925-26 was Rs. 218 crores. Though exact figures are not available rough calculations show that about 50 lakhs of tons are annually carried by ships engaged in the coasting trade of India. This volume is capable of further extension if harbour facilities are improved and the co-operation of railways ensured. The growth of an Indian Mercantile Marine controlled predominantly by Indians ought to stimulate the coastwise trade, as also the present government policy of improving the harbour facilities evidenced by the schemes of development already set on foot at Vizagapatnam and Cochin. This stands in favourable contrast with the policy of official negligence of old ports like Suart and Broach, which have been allowed to be silted up.

The total value of the sea-borne trade of India was estimated at Rs. 682.15 crores in 1925-26. Confining ourselves only to the five principal ports of India, viz., Karachi, Bombay, Rangoon, Madras and Calcutta, where nearly five-sixth of the trade is concentrated, about 120 lakhs of tons per year are carried. In spite of this big volume of trade the Indian share in it is almost contemptible especially. It has been estimated that the share of Indians in the coasting trade amounts only to 13 per cent, and in the oceanic trade, only 2 per cent. In this connection the following figures regarding the number, tonnage and nationality of the vessels engaged in the foreign sea-borne trade of India which entered and cleared at the ports in British India, are illuminating.

* See Digby : op. cit. pp. 87-89 and Malaviya's Minute of Dissent to the Industrial Commission's report, pp. 299-300. As Mr. Digby "shows the Indian Tonnage in 1898-99, compared with British and foreign in 1857, is one seventieth of the whole trade now against one half then."

Nationality of vessels	Pre-War Average		War Average 1926-27.				Percentage share of each nationality in total tonnage in 1926-27.
	No.	Tons (1,000)	No.	tons (1,000)	No.	tons (1,000)	
(i) Entered							
British ...	2,478	6,140	2,272	4,249	2,048	5,745	68.8
British Indian ...	312	171	320	112	327	114	1.4
Foreign ...	636	1,738	592	1,269	692	2,429	29.1
Native Craft ...	890	67	1,476	119	627	58	.7
Total entered ...	4,316	8,116	4,660	5,749	3,694	8,346	100
(ii) Cleared							
British ...	2,456	6,182	2,309	4,432	2,118	6,052	69.6
British Indian ...	322	183	298	70	346	127	1.5
Foreign ...	615	1,672	594	1,277	765	2,459	28.3
Native Craft ...	858	63	1,728	146	587	56	.6
Total cleared ...	4,251	8,100	4,929	5,925	3,756	8,694	100
Grand Total ...	8,567	16,216	9,589	11,674	450	17,040	.....

These figures show that even of the paltry 2 per cent of the trade in the hands of Indians nearly 35 per cent is accounted for by small native craft. Nor is there any evidence of progress from year to year. All this means the loss of a highly remunerative branch of business to the country. The total shipping earnings have been estimated at Rs. 57 crores, of which 50 crores are carried away by foreign steamship companies, Rs. 9 crores in coastal traffic, Rs. 38 crores in sea-borne traffic and Rs. 3 crores in passenger business.*

* See Haji : *Economics of Shipping*, pp. 317-332 and p. 375.

The monopoly of the coastal trade which is controlled by a "Conference" of a few big British Navigation Companies has created a very uncomfortable position for Indian shippers as well as ship-owners. As the high profits of over 20 per cent on the paid-up capital earned by these Companies show, fairly high freight rates are being charged to the shippers, which ultimately have to be borne by the Indian consumers. Moreover, as the Fiscal Commission point out, the great disparities of rates between the charges on goods shipped from one Indian port to another and those on goods conveyed between India and foreign countries handicap Indian goods in transmission in comparison with goods from foreign countries, and neutralise the natural protection which an industry might expect to receive in its own country by reason of the distance of foreign manufacturing centres.* But even more serious evils of this foreign monopoly of the coasting trade of India are those connected with the organised and successful attempts made by this Conference to suppress indigenous shipping enterprise in its infancy by methods which may be held to result in unfair or cut-throat competition. The two most important grievances of Indian ship-owners are; (1) The Deferred Rebate System; and (2) Rate Wars.

§ 29. **Deferred Rebate\$ Rate Wars etc.** :—The Deferred Rebate System has been thus explained: "The companies (shipping) issue a notice or circular to shippers informing them that, if at the end of a certain period (usually four or six months) they have not shipped goods by any vessels other than those dispatched by members of the Conference, they will be credited with a sum equivalent to a certain part (usually 10 per cent) of the aggregate freights paid on their shipments during that period, and that this sum will be paid over to them, if at the end of a further period (usually four or six months) they have continued to confine their shipments to vessels belonging to members of the Conference. The sum so paid is known as a deferred rebate."† "This system is designed to ensure the continued

* Fiscal Commission's Report, para, 31.

§ For a fuller description of this system and shipping rings see Haji, op. cit., Chap. V.

† Haji, op. cit., p. 126.

'loyalty' to the shipper of the monopolistic shipping Conference, and deprives them of all freedom of dealing with regard to the shipping of his goods. What is more serious is that the deferred rebate system places a powerful weapon in the hands of the monopolists for throttling any indigenous shipping enterprise. The Fiscal Commission strongly recommend legislation on the lines followed in other countries against this system. It is not a valid objection against this to point out that the deferred rebate system acts equally powerfully against new competitors of every nationality and not only against those of India. For, competitors of other than Indian nationality can usually count on support from their own governments in the form of subsidies and direct bounties for ship-building, and also their own coastal trade is generally reserved for them.

As regards the British shipping companies, they already occupy a position of substantial, practically unchallenged, supremacy, and some of them are further helped by Government patronage in India in respect of mail subsidies and the carriage of Government stores. No such governmental assistance has been extended to indigenous shipping. In addition to the deferred rebate system the foreign shipping rings also use another weapon, viz., heavily underselling the Indian competitors with a view ultimately to raise the rates to a higher level than before, after the rivals have been ousted.* It is no matter for surprise, therefore, that attempts made by Indian enterprise during the last 30 years or so

*Some remarkable cases of rate wars were mentioned in the Assembly debates on Mr. Haji's bill for the reservation of Coastal Shipping (September 1928). It was stated by Lala Lajpatrai that the Bengal Steam Navigation Company, Ltd., which started with a capital of Rs. 10,00,000 in 1922, was killed by competition, because the foreign companies reduced their freights from 12 to 2 and afterwards raised them to 14. When the New Bengal-Burma Steam Navigation Company started with a capital of 25,00,000, the foreign competitors already in the field reduced the passage rates from 14 to 4 and freights from 17 to 4. The Scindia Steam Navigation Company—the most successful example of Indian shipping enterprise in recent years—was the victim of a similar rate war but has barely managed to survive by entering into an agreement with some of the foreign coastal shipping companies. (See also Haji, *op. cit.*, pp. 153-154.)

to enter into the promising field of shipping have, generally speaking, ended in irretrievable failure, and most of the companies formed for the purpose have been driven to liquidation. Another handicap under which Indian shipping enterprise is said to labour is the unfair treatment meted out to Indian Shipping Companies by the European Insurance Companies, who, it is alleged, put into the second class even those Indian ships that are regarded as first-class risks by experts in London solely on the ground of their Indian ownership.

Other disadvantages of the foreign monopolies in shipping may be briefly noticed. The foreign shipping companies often grossly neglect the comforts of the deck passengers on the coastal ships, whose grievances have formed the subject of inquiries by several Committees. Also, though the crews of the coastal and ocean-going steamers are largely Indian in composition, the number of Indians occupying the higher posts is negligible, and very few of the foreign shipping companies have hitherto shown any readiness to entertain Indian apprentices so as to enable them to qualify themselves as executive officers and engineers on the ships.

§ 30. The Position of the Indian Ship-building Industry :— The Indian ship-building industry is in no better position than Indian shipping. It is stated that the number of ships of hundred tons gross or over, built in the world in the ten years previous to the War, was nearly 17,000, their total gross tonnage being roughly over 28 millions. These figures will have to be considerably increased to arrive at the total tonnage of the same description built up-to-date. The total contribution of India, before and after the War, amounts to only 22 ships.* Competition with non-Indian ship-builders is only practicable at present for small vessels owing to the cost of bringing out such vessels to India, which is large in proportion to their price. Elsewhere the foreign ship building yards hold undisputed sway. There are no suitable ship-

* See letter from the Marwadi Chamber of Commerce, Bombay, to the Government of Bombay, Marine Department, supporting Mr. Haji's Bill for the Reservation of Coastal Trade.

building yards in India for large ships and the few repairs shops that exist are controlled by non-Indians.

§ 31. The Need for an Indian Mercantile Marine :—The deplorable position of the Indian shipping and ship-building industries has excited much uneasiness in non-official circles for several years past. The arguments advanced in favour of extending special protection to these industries aim at showing that they satisfy the conditions laid down under the policy of discriminate protection. Thus it is argued that India possesses undoubted facilities for shipping and ship-building, also that elsewhere, e.g., in Japan, the United States and Germany, state intervention has been the prime factor which has been responsible for endowing these countries with powerful mercantile marines within a remarkably short period. * Even England's maritime greatness is often attributed to the protection derived from the Navigation Acts which were in operation for well-nigh two centuries before they were repealed towards the middle of the last century. Lastly, the collapse of most of the attempts made by Indian shipping enterprise to contest foreign monopoly even in home waters has been naturally offered as a convincing argument for determined state intervention.

The great need for a mercantile marine in India is easily proved. Apart from the removal of the handicaps already mentioned, under which Indian ship-owners, shippers and the deck passengers are labouring at present, there are several other positive advantages to be considered. The value of a mercantile marine as a naval auxiliary and a second line of defence in times of war is universally recognised, and as India has now just recently laid the foundation of her own navy (The Royal Indian Navy), she cannot afford to neglect this aspect of the question. Again, India's coastal and foreign sea-borne trade is sufficiently large in volume to keep an Indian mercantile marine busy. Her dependence on foreign shipping companies—the inconvenience of which was brought home particularly during the

*For a detailed treatment of the various forms of state-aid to indigenous shipping and ship-building in these and other countries see Mr. Haji's Pamphlet on State Aid to National Shipping.

War, when there was a great shortage of tonnage—is an element of weakness in her economic position as also in that of the Empire at large. Moreover, the proper development of a mercantile marine will open new avenues of employment to Indians. Navigation, Marine Engineering and Insurance are highly remunerative branches of business, but to-day their doors are practically barred and bolted against Indians. The argument that Indians have no aptitude or liking for a sea-going career is unconvincing and is belied by India's record in the past. It is also unfair to urge it since no chance has so far been given to Indians to prove their fitness in this part of the field. It is further useful to remember that, not very long ago, a similar charge used to be made against the Germans, who as everybody now agrees, are second to none in the qualities required for seamanship. And it is significant that the Mercantile Marine Committee do not anticipate any difficulty in getting educated men of good character as apprentices to the sea if the prospect of ultimate promotion as officers in the Mercantile Marine is held out to them.

§ 32 The Mercantile Marine Committee (1923) :—In response to the persistent agitation in favour of an Indian Mercantile Marine, Government at last made a move in the matter, and in pursuance of a resolution moved by Sir Sivaswami Iyer in the Assembly, appointed the Indian Mercantile Marine Committee in February 1923, to consider and report what measures were necessary for the promotion of the Indian shipping and ship-building industries. The main recommendations of the Committee may be summed up as follows:—

(1) In order to provide both for the training and future employment of the officers, indispensable for the formation of an Indian Mercantile Marine, a training ship and tender should be established at Bombay by Government. (Government have accepted this recommendation and have decided to utilise the Royal Indian Marine Vessel ' the Dufferin ' as a training ship for deck-officers and engineers of the Indian Mercantile Marine, and the necessary steps have been taken to refit her so as to enable her to take in cadets.) (2) For the training of marine engineers provision should be made at the Colleges of Engineer-

ing and facilities should be given for further experience at sea. (3) The coastal trade should be reserved for ships, which are to arrange for eventual indianization as regards ownership and controlling interest. This is to be effected by the introduction of a system of licenses or permits as in Australia. The following qualifications should be laid down for eligibility for a license to a shipping company:—(a) That it is registered in India; (b) that it is owned and managed by an individual Indian or by a Joint-Stock Company (public or private), which is registered in India with a Rupee Capital and with a majority of Indians on its Directorate and a majority of its shares held by Indians; and (c) that the management of such a Company is predominantly in the hands of Indians. In course of time other conditions should be laid down, e. g. that the officers and crews should be entirely Indian, and that the ships applying for licenses should have been built in India. Also, from a certain date to be specified by Government, all ships should be required to give an undertaking regarding the employment of Indian apprentices and the gradual indianisation of their officers and engineers. The licensing authority may also be vested with power to take such steps, with the approval of the Government of India, as may be considered advisable to deal with deferred rates, rate wars or any other conditions which act as an undue restraint on trade. (5) Arrangement should be made by the Government of India to purchase one of the existing British lines operating on the coast as a going concern and appoint directors to control it, the majority of whom should be Indians. Eventually the ownership of vessels in these lines should be transferred to approved Indian owners with a view to the above concern ultimately being placed in the hands of Indian companies. (6) The question of granting navigation bounties to purely Indian shipping companies in respect of overseas trade to other countries should be favourably considered at some future date, as soon as a sufficient number of trained Indian officers are available and Indian ship-owners have proved efficient in managing and running coastal steamers. (7) In case the license system recommended by the Committee is found to be inconsistent with the British Merchant Shipping Act of 1884, resort should be had to a

system of bounties on navigation to all Indian-owned and Indian-managed ships and the grant to them of mail contracts and preference for the carrying of Government stores. (8) Calcutta should be developed as a centre of self-propelled ship-building, being most suitable owing to its vicinity to coal and steel-producing districts and the greater experience which it commands than any other centre. The Committee recommend that protection should be given to the industry in the form of construction bounties so as to make up the difference between the minimum cost of production in India and abroad, subject to a maximum of 25 per cent of the price abroad. (9) The establishment of a ship-building yard by an Indian Company* may be aided by Government by (i) cheap loans and assistance in acquiring suitable sites, (ii) extension of Government and Port Trust patronage on certain terms regarding cost and (iii) legal provision that when such a suitable ship-building yard is completed and established, all ships seeking a license on the coast should also be required to have been built in India. (10) Expert assistance from abroad for ship-building should be invoked to start with. India must, however, establish schools and colleges in the country itself for the study of naval architecture as in England. In this matter she must follow Japan and the United States, and men should be sent out to Britain to take instruction in the schools and ship-yards there, so as to enable them to become teachers and leaders in the industry after they return. In the meantime the Colleges of Engineering should be strengthened and provide for additional post-graduate courses in Naval Architecture.

§ 33. Bill for Reserving the Coastal Traffic for Indian Shipping :—In the September Session (1928) of the Assembly, Mr. Haji moved his Bill for the Reservation of Coastal Traffic. It makes provision for 75 per cent of the stock to be vested in British Indian nationals and 75 per cent of the Directors on the Board in the case of a Joint Stock Company to be such nationals. The

* The Hon'ble Mr. Lallubhai Samaldas prefers that ship-yards should be laid out and run by Government to be sold later on by tender as going concerns.

Bill has been referred to a Select Committee with instructions to report by February 1929. It evoked a good deal of opposition from the Government Benches and several European members of the House. It was contended, among other things, that the proposal in the Bill was economically unsound and was not in the interests of India. It was also urged that it was unfair to Burma. As regards the last point, it must not be forgotten that Burma is a part of British India, and it is a vicious principle to consider a question of national importance from a parochial provincial point of view.*

The principle of reservation of coastal traffic contained in the Bill has been adopted practically by all nations with aspirations of developing their own mercantile marines, and India would do well to take a leaf out of their book in this matter. While, like every other measure of protection, the reservation of the coastal traffic for Indian ships is bound to be expensive for a time to the country, its justification is the familiar one, viz., the confident expectation that protection will before long be unnecessary, for under its invigorating influence Indian enterprise will soon be in a position to serve the needs of the country much more effectively than is the case today.\$

Regarding the treatment of existing vested interests, leaving aside the drastic step of expropriation, one of two methods may be adopted. Either the existing lines might be bought over by Government with a view ultimately to handing them over to Indian Companies, or they might be offered the option of gradually undertaking to indianize themselves within a period of five

* If it is also worth while mentioning that a Burman member of the Assembly protested that the argument about the possibility of Burma suffering is supported by the officials and not by the Burmese public.

\$ Mr. Haji has worked out interesting details to show that the reservation of coastal traffic is not at all an unworkable proposition. He estimates that taking the average tonnage of a steamer to be 6,000, the employment of 100 steamers will suffice for the coastal trade. He holds that a capital outlay of Rs. 16.50 crores would suffice for the purpose and points out that this is only equal to about 1/10th of the amount (Rs. 150 crores) recently provided for by the Government of India for the development of Indian railways. If the process of reservation is completed during five years, only 20 steamers need be purchased by India during each one of those years. See Haji: *op. cit.*, pp. 374-375.

years or so, so as to make them eligible for operating on the coast. After all, it must be remembered that coasting trade is a domestic preserve under International Law, and in this matter Indian interests ought to be considered first and last.

As regards the ship-building industry we are in agreement with the recommendations made by the Mercantile Marine Committee for promoting it and think that they should be put into execution without any further delay.

CHAPTER VII

THE TRADE OF INDIA.

This chapter will deal with the trade of India and for the sake of convenient treatment the subject may be divided into its main branches as follows:—(1) External Trade consisting of (a) Sea-borne Trade, (b) Enterpot Trade, (c) Transfrontier Trade, and (II) Internal Trade including Inland and the Coastal Trade.

I. EXTERNAL TRADE.

§ 1. A Historical Retrospect:—The early history of Indian trade may be dismissed briefly, our primary concern being with its development in the modern period since the middle of the last century. There is ample evidence of India's trade relations in ancient times with distant lands. As long ago as 3000 B. C. India had trading connections with Babylon. Egyptian mummies belonging to 2000 B. C. are supposed to have been found wrapped in Indian muslin of the finest quality. "There was a very large consumption of Indian manufactures in Rome. This is confirmed by the elder Pliny who complained that vast sums of money were annually absorbed by commerce in India. The muslins of Dacca were known to the Greeks under the name of *Gangetika*."* Among other countries with whom India traded were China, Persia, Arabia, etc. The trade of India, as indeed all ancient trade, was in rare and costly commodities of comparatively great value in small bulk in contrast with the present-day trade characterised by transport over large distances of cheap and bulky commodities catering for the needs of the masses. The principal articles of exports were textile manufactures, metalware, ivory, perfumes, dye-stuffs, spices etc., and the imports consisted of minerals of which there was a deficiency in India, such as brass, tin, lead, and also wines, horses etc. There was a net import of a large quantity of gold which suggests an excess of exports over imports—a feature which

* Malaviya's Minute of Dissent, op. cit, p. 295.

has all along characterised India's trade with other nations. There was also a certain amount of entrepot trade chiefly in silks and procelain previously imported from China, in pearls from Ceylon, in precious stones from the Indian archipelago. This entrepot trade may be taken as a token of India's possession of a fleet of merchant-men.

During the Mahommedan period, which may be said to have commenced from the 11th century, certain new influences came to act upon the foreign trade of India. The early Mahommedan period being more unsettled than the preceding Hindu period must have adversely affected India's trade development. On the other hand, the communications established with India through the North-West Frontier stimulated the overland trade of India. As Moreland points out, there were two regular routes on the frontier from Lahore to Kabul and from Multan to Kandahar. "Kabul was a large commercial centre, and a meeting-place for merchants from India, Persia, and countries to the North, while it lay on the route from India to the main caravan road between Western China and Europe; Kandahar as the door-way from India to the greater part of Persia; and both routes carried a considerable volume of traffic when judged by standards appropriate to the conditions prevailing at the time."* Moreover, the means of transport in the Moghul period were more satisfactory than before. There were a number of fairly good roads. Also, the river-system of the country, especially in the North, was fully availed of for the purpose of trade and there was also a brisk commerce on the coast line of India. Moreover, the patronage of the Moghul courts, imparted a considerable stimulus to Indian industries, particularly to those which produced luxury goods. The shipping trade was largely controlled by the Moslems, especially on the Malabar coast and to a lesser extent in the Gulf of Cambay and the Coromandel coast, which later came to be largely in the hands of the Banias and Chetties. Malabar was the great entrepot for almost the whole trade of the Indian seas coming from the far East and the Red Sea, Calicut being the principal port for this trade. During the Mahommedan period the general course of trade remained unchanged

* See Moreland : *India at the Death of Akbar*, p. 219.

and "Gibbon's mordant aphorism 'that the objects of oriental traffic were splendid and trifling', is in substance as applicable to the sixteenth as to the second century."* The imports were principally gold for coinage and display, horses were imported in large numbers and metals, such as copper, tin, zinc, lead and quicksilver; also luxuries like amber and precious stones. In payment for these imports India sent out her various textile fabrics, dye-stuffs like indigo, opium and other drugs, pepper and a few minor spices etc.

Towards the end of the 15th century came the epoch-making changes in the trade routes due to the discovery of an all-sea route to India *via* the Cape of Good Hope, which established the fateful contact between the East and the West. Till then the direct trade with Europe passed on the Indian Ocean as far as Aden, was then unloaded in the Gulf of Suez and carried by land and water to the Mediterranean Coast. It was thence taken up by the Italian traders of Venice and Genoa, who sent it further west by sea or to Antwerp by land over the Alps and then down the Rhine, at that period the chief distributor for Western Europe. It was the prospect of annexing the large profits of this trade at the cost of their enemies, the Venetians, and of propagating the Christian faith which inspired the Portuguese quest for a sea route to India. We are not concerned here with the subsequent rivalry among the various powers of western Europe, the Portuguese, the Dutch, the English and the French, nor with the ultimate triumph of the English and the establishment of their power in India. We have already said that it was the fine linens and calicoes, the jewels and embroideries and woollen and silk manufactures and not the raw materials which attracted European traders to India and supplied the basis for the lucrative trade of the East India Company securing for it the virtual monopoly of trade with the East owing to the elimination of the competition of the French as a result of the Seven Years' War. There was at one time considerable opposition in England to the trade of

* Moreland : op. cit., p. 196.

the Company with India, since Indian imports of calicoes and spices for which there was an insatiable demand in England had to be paid for by an export of specie.* to India, which was a poor market for the English woollens. This agitation became so keen towards the end of the seventeenth century that, from that time onwards, the use of Indian textiles in England was penalised either by complete prohibition, or heavy import duties. We have already stated that the commercial instincts of the East India Company led it at first to encourage Indian industries, on which its export trade depended, but that the pressure of the vested interests in England led to a reversal of this policy in the 18th century and India came to be looked upon primarily as a valuable source of raw materials necessary for developing the manufactures of England which were rapidly expanding during the period of the Industrial Revolution. We have also referred to the various causes of the decay of the indigenous industries of India and traced the process of its ruralisation during the latter half of the 19th century.

All this did not fail to exercise a far-reaching influence both on the direction and the nature of India's foreign trade. The first half of the nineteenth century witnessed a remarkable change in the character of the trade between India and England. Henceforward, India began to receive those very commodities as imports which had hitherto bulked so largely in her export trade, viz., cotton manufactures and sugar. The Lancashire Cotton Industry had so developed that by the middle of the century imports of cotton piecegoods represented about half the total imports of foreign merchandise into India.†

§ 2. Sixty Years of India's Trade (1864-65 to 1926-27):—
The year 1869 when the Suez Canal was thrown open for navigation marks for all practical purposes the beginning of the modern period in the history of India's trade. The most striking characteristic of this period is the steady growth in the volume

* The acquisition of the Diwani of Bengal and the vicious system of investments (purchasing goods for export out of the Indian revenues) considerably reduced the export of bullion to India and lessened the opposition to the Indian trade.

† Cotton op. cit. p. 95.

of the export and import trade, though the pace of development has not been uniform throughout. The following figures are of interest in this connection :—

Value of Merchandise (including Government transactions) during the last five years with quinquennial averages for the past sixty years.* (in lakhs of Rupees).

Quinquennial average	Imports	Exports	Total
1864-65 to 1866-69	31,70	55,86	87,56
1869-70 to 1873-74	33,04	56,25	89,29
1874-75 to 1878-79	38,36	60,32	98,68
1879-80 to 1883-84	50,16	79,08	1,29,24
1884-85 to 1888-89	61,51	88,64	1,50,15
1889-90 to 1893-94	70,78	1,04,99	1,75,77
1894-95 to 1898-99	73,67	1,07,53	1,81,20
1899-1900 to 1903-04	84,68	1,24,92	2,09,60
1904-05 to 1908-09	1,19,85	1,65,44	2,85,29
1909-10 to 1913-14	1,51,67	2,24,23	3,75,90
1914-15 to 1918-19	1,59,25	2,25,83	3,85,08
1919-20 to 1923-24	2,67,05	3,06,38	5,73,43
in the year 1922-23	2,46,19	3,16,07	5,62,26
„ 1923-24	2,37,18	3,63,38	6,00,56
„ 1924-25	2,53,37	4,00,24	6,53,61
„ 1925-26	2,36,00	3,86,82	6,22,82
„ 1926-27	2,40,91	3,11,04	5,51,95

These figures show that exports increased from an average annual value of Rs. 55.86 crores for five years of trade during 1864-65 to 1868-69 to nearly Rs. 400 crores in 1924-25. During the same period imports rose in value from Rs. 31.70 crores to 53.37 crores. †

The chief causes of this growth, may now briefly be indicated. The establishment of peace and order with the practical completion of the British conquest of India by the middle of the last century supplied the much-needed security of life and property

* Review of the Trade of India, 1926-27.

† See also The Economic Resources of the Empire, edited by W. Worwick Article by Lindsay, the Indian Trade Commissioner.

for the development of commerce. Improved means of communication also opened up the country far and wide for trade. The part played by the railways and roads has already been noticed in the last chapter, to which may be added the influence of the development of telegraphic and postal communications. But far and away the most important single event was the opening of the Suez Canal which brought India nearer to England by about 3,000 miles. The Canal rehabilitated the Mediterranean route to the East and gave new opportunities to countries facing the Mediterranean such as France, Austria and Italy. The utility of this route was immensely improved by the laying of the submarine cables between Bombay and Suez. This together with the great improvement in naval architecture and the rapid growth of mercantile marines fostered by the various states gave a great fillip to India's trade with distant lands and permanently revolutionised its volume and character. The greater part of India's exports came to consist of articles of considerable bulk and comparatively low value, which could now be transhipped cheaply over thousands of miles so as to satisfy the growing international demand for them. Food-stuffs like wheat, rice and tea, and raw materials such as cotton, jute, oil-seeds, hides and skins came to be exported in ever increasing quantities,[†] and they were paid for by the imports of manufactures such as cotton piece-goods, machinery, hardware, railway materials, glassware etc., from England and later from other countries like Germany, the United States and Japan, where striking developments in manufacturing industry were taking place. Another factor which gave an impetus to the trade of India was the adoption of the policy of uncompromising Free Trade. The numerous internal customs barriers and transit duties which had so long impeded trade were swept away by 1853. The principle of Free Trade which had carried all before it in England about the middle of the last century was applied unhesitatingly to India. Almost all the export duties were abolished by 1874 and the discrimina-

[†] The agricultural policy of the Government in India was largely inspired by the idea of stimulating the export of Indian agricultural produce and the big irrigation schemes undertaken in the Punjab, U. P., and Sind were to a large extent in furtherance of this policy.

tion in favour of British against foreign shipping was removed. Free Trade, however, scored its greatest victory when, under pressure from Lancashire, all import duties with a few trifling exceptions were swept away in 1882.†

We may in this connection notice the deliberate and organised efforts made by several countries such as Germany and Japan, during the 25 years or so preceding the outbreak of the War, to establish direct trade relations with India and challenge the predominant position occupied by Great Britain in India's international trade. The large share of the United Kingdom,§ in India's trade during this period is easily accounted for. The establishment of the Company's rule in India, the discomfiture of rival European nations and the use of its political power by the Company for developing its trade in Indian goods have already been noticed. Though the Company's trade monopoly was abolished in 1813 and full freedom was given to all nationalities to establish commercial relations with India and though all foreign countries were gradually placed on a footing of equality with England in respect of shipping etc., the British people continued to be in practically monopolistic possession of the field until recently. During this long period the United Kingdom carried on a considerable entrepot trade in Indian produce distributing it among other European countries. The investment of British capital in Indian railways and other undertakings and the management of the railways by British Companies, British control of shipping and banking, the establishment of trade organisations in the country such as the British export houses and the European (British) Chambers of Commerce and the power of directing the fiscal policy of the country, were the principal factors which gave Britain an upper hand.

§ 3. The struggle for the Indian market:—This supremacy began to be gradually undermined in the closing decades of the

† It is true that the import duties had to be reimposed for revenue purposes in 1894 owing to the fall in the exchange value of the rupee which subjected the finance of India to a severe strain, but they were maintained at the general low rate of five per cent *ad valorem*.

§ For statistical details see section on Direction of India's Trade in this chapter.

last century. Germany was the first power to challenge it and was later followed by Japan whose interest in the trade with India was especially quickened after the Russo-Japanese War. The object of these powers was primarily to push the sale of their manufactures in India. But the organisation created for this purpose also served to stimulate Indian exports of raw materials and food-stuffs, which these countries required for their own industries. The principal methods adopted for this purpose were (1) the development of national shipping services, (2) the establishment of branches of national banks, such as the German Deutsche-Asiatische Bank and the Japanese Yokohama Specie Bank, which offered special credit facilities to their nationals, and (3) the establishment of foreign commercial houses at the principal centres of trade like Bombay and Calcutta. It is hardly necessary to point out that this activity had the full sympathy and support of the governments concerned and their Consulates in India did yeoman's service in fostering their country's trade with India. The United States, however, was for a long time content to deal with India through London and her efforts to promote direct trade relations were not so conscious and determined as those of Germany and Japan until after the out-break of the War.*

§ 4. The Pre-War position summarised :—The combined effect of all the factors noticed above was seen in an enormous growth of the export and import trade of India, though the figures given above show that the growth did not take place at a uniform pace throughout the period just reviewed. Up to 1873, there was a large increase in exports, especially between 1864 and 1869 owing to the American Civil War which led to large exports of cotton at high prices from India, while it checked the imports of piecegoods into the country owing to the difficulties of England in obtaining the usual supply of raw cotton. Between 1873 and

* The languid interest of France in the Indian trade is accounted for by the fact that her exports consisted mostly of luxury articles for which there was no large demand in India. See R. M. Joshi : *Indian Export Trade*, Chap. VII.

the end of the century trade development was comparatively slow.* This was largely due to certain special factors. In the first place, the rupee had been steadily losing its gold value and fell from two shillings in 1872 to about fourteen pence in 1893. The violent oscillations in the value of the rupee introduced an element of uncertainty and speculation in the foreign trade with gold-standard countries and served to check its normal growth. Moreover, the famine of 1876-78 and the two others which occurred at the end of the century and the repeated visitations of plague, which first appeared in Bombay in 1896, aggravated the situation. Lastly, while the successful stabilisation of the rupee at 1s 4d between 1898 and 1914 smoothed the course of India's trade with gold standard countries, the appreciation of the rupee contributed, to some extent, as we have already seen, to the loss of trade in textiles with Japan and China.

The first fourteen years of the new century witnessed a remarkable expansion of the foreign trade of India, especially since 1905. The largest increase was revealed by the five years preceding the War for which the average was Rs. 224. 23 crores for exports and Rs. 151. 67 crores for imports as against Rs. 124. 92 for exports and Rs. 84. 68 for imports during the quinquennium 1899-1900 to 1903-04. During these years the rupee was almost stable, public works such as railways and irrigation were being pushed forward with vigour, there were no serious famines such as those at the end of the last century, and the virulence of plague was decreasing. Moreover, as already stated, Germany and Japan, and to a lesser extent the United States, were making organised efforts to push their trade which was fast expanding under the stimulus of the economic transformation which they were undergoing, bringing them into line with England as industrial nations.

§ 5 Effects of War on India's Trade:—The following tables* bring out the effects of the War on India's trade:—

* Prof. R. M. Joshi in his '*Indian Export Trade*' (p. 8) shows that between 1834 and 1855 exports rose from 8 to 23 crores of rupees, and between 1855 and 1873 from 23 to 60 crores. Between 1873 and 1893, the rise was only from 60 to 100; then till 1899 there was practically no rise at all; and it was only between 1899 and 1914 that there was the striking rise from 100 to 203 crores of rupees.

† See Panandikar, op. cit. pp. 44-45.

TABLE I.

Value of the over-seas trade in total merchadise in £.million.

	1913-14	1914-15	1915-16	1916-17	1917-18	1918-19
Imports	127.5	96.5	92.1	106.8	109.6	125.7
Exports	166.0	121.4	133.0	167.9	163.3	170.2

TABLE II.

Value of the overseas trade (total merchandise calcutated at the prices current), in 1913-14. (£ millions)

	1913-14	1914-15	1915-16	1916-17	1917-18	1918-19
Imports	127.5	95.6	73.1	62.8	51.9	46.9
Exports	166.0	119.0	129.1	140.9	130.6	113.5

In order to ascertain the effects of the War on the volume of trade it is necessary to take into consideration the rise in prices which took place during the War years. This particularly applies to the imports which rose in value much more than the exports. Taking the prices of exports and imports in 1913-14 at 100, while the prices of imports rose to 268 those of exports rose only to 150 in 1918-19. Even taking into consideration the recorded values of exports and imports the tables above show that both the branches of foreign trade received a set-back on the outbreak of the War and that, while the value of the exports recovered from 1916-17 onwards, that of imports lagged behind the pre-War year even so late as in 1918-19. Table II, however, shows that there was a far more serious reduction in the volume of trade, especially of the import trade, which declined continuously throughout the War years. We may now briefly examine the causes which brought about this state of affairs. The War led to a complete cessation of trade with the enemy countries. The discontinuance of trade with Germany was particularly serious for she had been India's best customer after Great Britain in the pre-War period. At the same time the trade with the

allied countries like Great Britain, France, and Belgium could not be maintained at the pre-War level owing to their preoccupation with the War. Trade with neutral countries was subjected to restrictions calculated to prevent munitions of war from India reaching Germany through such countries and to make Indian supplies solely available for the allies. A more distressing factor was the sharp rise in freights as a result of the disappearance of enemy tonnage from the high seas and the pressure of war requirements on the remainder available. The tonnage difficulty particularly affected India owing to her being separated by a greater distance from Western Europe than other suppliers of raw materials to Europe like the Argentine Republic, Brazil, Canada, and the United States of America. This factor largely discounted the advantage which India might otherwise have derived from the great demand in Europe for her commodities. The dislocation in the foreign exchanges and the insecurity on the sea owing to the destructive activity of the 'Emden' and the 'Konigsberg' were also factors which disturbed the course of trade. The country, however, soon began to adapt itself to war conditions. Large quantities of sand bags for trench warfare and hides for the manufacture of boots for the soldiers were required, which greatly stimulated the exports. The export trade would have shown an even larger increase had it not been for the difficulties regarding export finance arising from the curtailment of the sale of Council Bills and from government control. Though the import trade did not experience the same revival, the gap caused in the Indian market was partly filled up by increased imports from the United States and Japan who fully exploited the situation so created to their own advantage. Thus the War affected Indian trade more adversely than the trade of some other countries like Japan. "While India's trade was painfully endeavouring, till the cessation of the hostilities, merely to recover from the adverse effects of the war, making it futile to expect its expansion, Japan's export trade had more than trebled and her import trade had increased $2\frac{1}{2}$ times by the time of the Armistice."*

* Panandikar, op. cit. p. 55.

One welcome feature, however, of India's war-time foreign trade was the increase in the exports of manufactures whose percentage to the total export trade rose from 22.4 per cent in 1913-14 to 36.6 per cent in 1918-19, though much larger increases were recorded in the case of other countries like Canada. The artificial stimulus given by the War to Indian industries like cotton, jute, leather, steel and iron has already been noticed, and this accounts for the increase in the exports of manufactures, which, however, might have been much higher if India had been fully prepared to take advantage of the temporary disappearance of foreign competition in her markets. It is necessary in this connection to supply a corrective to the common notion that the War brought immense prosperity to India. The abnormal increase in her favourable balance of trade was not an indication of prosperity but rather the reverse. It had the effect of inflating the currency by the addition of a large volume of paper money and rupee coinage.* The enforced reduction in imports occasioned very serious inconvenience and though a few traders, especially in capital towns, seemed to be making more money than they quite knew what to do with, there is no proof of a general rise in the standard of life and it is quite certain that the phenomenal rise in prices adversely affected a large number of people.‡

§ 6. Post-War Trade 1919-1920 to 1926-1927:—The following figures may serve as an introduction to a discussion of the post-War developments in trade:—

Value of sea-borne trade in total merchandise (including Government stores.) (In crores of Rupees.)

	1919 -20	1920 -21	1921 -22	1922 -23	1923 -24	1924 -25	1925 -26	1926 -27
Imports	221.70	347.57	282.59	246.19	237.18	253.37	236.00	240.91
Exports	336.02	267.76	248.65	316.07	363.37	400.24	386.81	311.04
Net ex- ports of merch- andise	114.31	79.80	33.93	69.88	126.10	146.87	150.81	70.13

* For a fuller treatment of the question see the Chapters on Indian Currency and Exchange.

‡ See Panandikar, op. cit. pp. 46-47.

As in a number of other countries so in India, the early post-War period was characterised by a trade boom caused by the removal of many of the War-time prohibitions on exports as well as a gradual resumption of commercial intercourse with enemy countries accompanied by an improvement in the freight position. There was also a brisk demand for Indian produce on the part of the Western countries for the reorganisation of their industries. The revival of trade, especially on the side of exports, would have been even more striking but for the railway congestion in India, high prices, labour troubles, unstable foreign exchanges, the rise in the exchange value of the Rupee and the continuation of the restrictions on the export of cereals due to the failure of the monsoon in 1918-19. Even as it was, however, the pace of the post-war boom was too fast and it was inevitable that before long it should be succeeded by a slump, indications of which were clearly apparent in the latter part of the year 1920-21. The export trade was the first to be affected. The markets of Great Britain, the United States and Japan, who were all among India's best customers, being glutted with Indian produce, there was a considerable slackening of the demand on their part. Central Europe, which had been a valuable market for Indian exports during the pre-War period no doubt badly wanted Indian products, but could not buy them owing to their shattered resources and reduced purchasing power. The continuous inflation of their currency and its unexampled depreciation in terms of foreign currencies combined with their inability to command credits abroad made matters still worse for them. The unsatisfactory rains of 1920 in India and the high prices of food-stuffs necessitated the continuance of the embargo on the exports of food-stuffs. There was also a severe crisis in Japan which checked the exports of Indian cotton to that country. The ill-fated attempts of Government to stabilise the exchange value of the rupee at 2s gold, on the recommendation of the Babington-Smith Committee,* further paralysed the already weak export trade. The import trade, on the other hand, expanded rapidly. India's import requirements had been starved during the War and

* See Chapters on Currency and Exchange.

orders had been placed for machinery and other manufactured goods during the War and after the Armistice for delivery at the discretion of the manufacturers, and these now began to pour into the country. The high exchange also gave a powerful stimulus to the import trade and orders were placed for immense quantities of foreign manufactured goods. It is no matter for surprise, therefore, that there was a heavy balance of trade against India to the extent of Rs. 79.80 crores in 1920-21, which continued into the next year when it amounted to Rs. 33.93 crores. The year 1921-22 was one of unrelieved depression, when heavy losses were incurred by the importers as a result of the collapse of the rupee and a failure to stabilise it at 2s. (gold).

Since the year 1922-23 a recovery has been discernible. Although it has been tardy in making itself felt, so far as the import trade is concerned, the general trend towards the restoration of normal healthy conditions has been continuously in evidence.* The conditions which have favoured the progress towards gradual recovery have been the progressive stabilisation of the European currencies and the improvement in the credit position of the Central European countries and the settlement of the reparations question by means of the Dawes Scheme in 1924. The League of Nations, it may be noted here, has played a beneficent part in hastening the process of restoration e. g. by helping Austria and Hungary in the work of currency stabilisation. In spite of the amendment of the situation, however, it is still far from being entirely satisfactory owing, among other things, to the fact that the international financial problem still dominates the situation and Europe is not yet rid

* 1924-25 was a record year for the Indian export trade. Stocks of Indian goods in foreign markets were low at the beginning of the year, demand was strong and there was a general rise in the sterling price of Indian exports the rise in most cases being appreciably greater than the rise in the sterling value of the rupee to 1s 6d in 1924-25. The import trade improved also, but not to the extent anticipated. The fall in the value of the exports in 1926-27 was mainly the result of a fall in the quantity as well as value in the exports of raw cotton, and fall in the value of the exports of raw and manufactured jute due to the previous year's high range of prices not being maintained. There was also a fall in the shipments of rice wheat, barley and oilseeds.

of her War-time legacies of tariff barriers with rapid fluctuations in the tariff rates, and the contraction credit, of production and of purchasing power. It is as yet too early, therefore, to look for any substantial and steady world-wide expansion of industry and trade.

The following table indicates the course of India's trade (values of imports and exports of merchandise) during the post-War years on the basis of the declared values in 1913-14 :—

(in crores of Rupees)

	1913 -14	1919 -20	1920 -21	1921 -22	1922 -23	1923 -24	1924 -25	1925 -26	1926 -27
Imports ...	183	101	142	124	138	120	137	143	156
Exports ...	244	198	172	182	214	240	250	246	228
Total trade of merchandise excluding re-exports ...	427	299	314	306	352	360	387	389	384

This table shows that the export trade had either approached or regained the pre-War level in the three years 1923-24 to 1925-26, and that it was less active in 1926-27; also that the import trade, while it recorded distinct advance in 1926-27, is still a good way off from the pre-War level. A comparison of the values given in the preceding table with the actually recorded values for each year gives the following index numbers for imports and exports* :—

	1913 -14	1919 -20	1920 -21	1921 -22	1922 -23	1923 -24	1924 -25	1925 -26	1926 -27
Imports ...	100	06	237	214	169	190	180	158	148
Exports ...	100	198	140	127	140	145	154	152	132

* Review of the Trade of India, p, 4

These figures show that the level of prices for imports was distinctly higher than that for exports and partly explains why the import trade has not yet approached the pre-War level. Though some approximation in price levels took place in 1925-26, the figures for 1926-27 revealed again an increase in the margin of prices for imports and exports. The higher level of prices for imports means that India has to export more goods for obtaining a given quantity of imports.

§ 7 Characteristics of India's Sea-borne Trade:—We may now proceed to examine the principal characteristics of India's sea-borne trade. Tables I and II below mention the value of imports and exports of private merchandise according to five main classes; while tables III and IV show the comparative importance of the principal articles imported into and exported from British India respectively ;—

TABLE I.

Value of imports, (private merchandise,) according to five main classes. (In thousands of Rupees).

	Pre-War average	War average	Post-War average	1926-27
1. Food, drink and tobacco ...	21,84,65	26,38,94	37,82,25	38,36,40
2. Raw materials and produce and articles mainly un-manufactured ...	10,08,02	9,87,70	19,00,67	20,50,64
3. Articles wholly or mainly manufactured ...	1,11,78,79	1,08,23,85	1,92,55,46	1,68,30,64
4. Living animals ...	43,67	15,88	24,50	41,85
5. Postal articles not specified ...	1,69,59	2,77,82	4,41,85	3,72,05
Grand Total ...	1,45,84,72	1,47,80,19	2,54,04,73	2,31,31,58

TABLE II.

Value of exports, (private merchandise) according to five main classes. (In thousands of Rupees)

	Pre-War average	War average	Post-War average	1926-27
1. Food, drink and tobacco ...	62,96,53	59,56,95	59,62,99	74,56,47
2. Raw Materials and produce and articles mainly un-manufactured ...	1,04,66,38	86,41.03	1,45,90,86	1,38,67,73
3. Articles wholly or mainly manufactured ...	50,61,01	68,44,39	77,96,48	85,20,95
4. Living animals ...	35,05	22,18	30,42	38,32
5. Postal articles ...	90,76	1,32,15	2,52,64	2,49,69
Grand total ...	2,19,49,73	2,15,96,70	2,86,33,39	3,01,43,16

TABLE III

Table III on the next page shows the comparative importance of the principal articles imported into British India in 1925-26 and 1926-27.

The above tables illustrate numerically the oft-repeated statement that the bulk of the exports from India consist of food-stuffs and raw materials and the bulk of the imports of manufactured articles. We have already explained above how this characteristic of India's present-day trade stands in marked contrast with her foreign trade up to the opening decades of the last century, and also the process of the transition from the one to the other. We have also discussed the question relating to the policy to be followed with regard to the export of food-stuffs and raw materials from the country. * Similarly in the preceding chapters hardly a single opportunity has been lost of insisting with all possible emphasis on the desirability of rapid industrial development in the country so as greatly

See vol. I. pp. 213-229.

(In lakhs of Rupees)

	1925-26	1926-27	percentage of proportion to total imports of merchan- dise in 1926-27.
Cotton and cotton goods	69,31	70,08	30.30
Metals and ores	25,37	23,85	10.31
Sugar	15,83	19,16	8.28
Machinery and mill work	14,88	13,63	5.89
Oils	10,60	9,18	3.97
Vehicles	5,74	6,39	2.77
Provisions and oilman's stores	4,64	5,50	2.38
Hardware	5,19	5,06	2.19
Silk, raw and manufactures	3,74	4,59	1.99
Wool, raw and manufactures	4,66	4,46	1.93
Instruments, apparatus and appliances	3,53	4,01	1.73
Liquors	3,33	3,52	1.52
Railway plant and rolling stock	4,99	3,26	1.41
Spices	3,28	3,12	1.35
Paper and pasteboard	2,81	3,08	1.33
Tobacco	2,13	2,56	1.11
Glass and glassware	2,59	2,52	1.09
Chemicals	2,02	2,44	1.06
Dyes	1,82	2,13	.92
Rubber	2,17	2,10	.91
Drugs and medicines	1,83	2,06	.89
Apparel	1,65	1,77	.77
Fruits and vegetables	1,57	1,61	.70
Soap	1,46	1,52	.66
Faints and painters' materials	1.29	1,44	.62
Salt	1,04	1,26	.55
Building and engineering mate- rials	1.19	1,23	.54
Haberdashery and millinery	1,09	1,13	.49
Precious stones and pearls, unset	1,24	1,06	.46
† All other articles	25,18	27,59	11.8
Total value of imports	22617	23131	100

† These include, grain, pulse and flour, earthenware and procelain, stationery, belting for machinery, matches, wood and timber arms, ammunition and military stores, tea, tea chests, toys and requisites for games, boots and shoes, toilet requisites, books, printed etc., umbrellas for fittings, living animals, cutlery, jute and jute goods, fish (excluding canned fish),

TABLE IV.

The following table shows the comparative importance of the principal articles exported from British India in 1925-26 and 1926-27. (In lakhs of Rupees.)

	1295-26	1926-27	Percentage of proportion to total imports of merchandise in 1926-27
Jute, raw	37,94	26,78	8,88
Jute, manufactures	58,83	53,18	17,64
Cotton raw and waste	95,91	59,14	19,62
Cotton manufactures	64	10,74	3,57
Grain, pulse and flour	48,03	39,24	13,02
Tea	27,12	29,03	9,63
Seeds	29,63	19,08	6,33
Leather	7,10	7,37	2,45
Metals and ores	7,28	7,20	2,39
Hides and skins, raw	7,23	7,17	2,38
Lac	6,90	5,47	1,82
Wool, raw and manufactures	4,59	4,68	1,55
Rubber, raw	2,94	2,60	,86
Oilcakes	2,10	2,52	,84
Opium	1,93	2,11	,70
Paraffin wax	1,59	1,84	,61
Wood and timber	1,95	1,62	,54
Spices	1,76	1,55	,52
Coffee	1,85	1,32	,44
Manures	1,17	1,25	,41
Dyeing and tanning substances	1,33	1,17	,39
Mica	1,04	1,08	,36
Fodder, bran and pollards	1,28	1,06	,35
Tobacco	1,11	1,04	,35
Coir	1,08	99	,33
Oils	1,79	95	,32
Foods and vegetables	83	89	,30
*All other articles	10,89	10,36	3,37
Total value of exports ...	374,84	30,143	100

jewellery also plate of gold and silver. coal and coke, manures, paper making materials, bobbins, tallow and stearine, flax, raw and manufactured; gums and resins, furniture and cabinetware, clocks and watches and parts.

* These include hemp, raw; coal and coke; fish excluding canned

to reduce her present dependence on the imports of manufactures from abroad.

Even long before the War, a slight improvement in this direction had taken place and the percentage of exports of manufactures to the total exports had shown a tendency to increase gradually, though the bulk of the exports, then as now, were in the form of raw materials and food-stuffs. During the War period, for reasons already explained, this percentage showed an appreciable increase from 22.4 in 1913-14 to 36.0 in 1918-19*

In spite of some improvement, however, it is clear, that the salient features of the trade of India remain essentially as described above.

§ A Broad Analysis of the Imports and Exports:—We need not here go into the details of the various items of the import and export trade of India. We have had a good deal to say about the export aspect of the principal crops of India, such as cotton, jute, tea, oil-seeds, rice, wheat and also of raw hides and skins. Also the position as regards the export of certain manufactures from India, such as cotton manufactures, tanned hides, jute manufactures etc. has already received detailed notice. Similarly the import aspect of cotton manufactures, sugar, steel and iron, paper, cement, chemicals, glassware, etc. has been dealt with while discussing the prospects of the various industries in India.

It will be seen from table III above that cotton piece-goods, continue to hold the place of honour on the import side. Next in importance are metals and ores. Our imports of sugar which not long ago held the second place immediately after piece-goods, are still worth nearly 20 crores of rupees annually. Machinery and mill work, oils and vehicles, especially motor cars, hardware, etc. are other articles of substantial importance which are imported into the country.

On the export side, jute and cotton are the most important commodities. The exports of raw cotton contributed as much as 28 per cent of the total value of all merchandise exports in 1923-24, and 25 per cent in 1925-26. The lower percentage, viz., 19.62 in 1926-27 was due to the fall in the quantity and the value of

fish ;) provisions and oilman's stores ; animals, living ; drugs and medicines ; silk raw and manufactures ; fibres for brushes and brooms ; apparel ; cordage and rope, tallow, stearine and wax, bristles, saltpetre, candles, horns, tips, sugar etc.,

* See vol I, pp. 183-184

the exports of cotton. The next most important articles are food-stuffs, such as grain, pulse and flour, which contributed 13.02 to the total value of exports of merchandise, and tea which contributed 9.63 in 1926-27. In the same year, oil-seeds accounted for 6.33 per cent. Other principal articles of export are leather, metals and ores, hides and skins, lac, wool, etc.

The following tables show the variations in the shares of the principal articles in the import and export trade of British India in 1925-26 as compared with the averages of the pre-War and War periods.

Imports (percentages)

	1909-14 average	1914-19 average	1925-26
Cotton Manufactures	36	35	29
Iron and Steel	7	7	8
Machinery	4	3	7
Sugar	9	10	7
Railway Plant	4	2	2
Hardware	2	2	2
Mineral Oil	3	3	4
Silk	2	2	1
Other articles	33	36	40
	100	100	100

Exports (percentage)

	1909-14 Average	1914-19 Average	1925-26 Average
Jute, raw and manufactures	19	25	26
Cotton, raw and manufactures	21	21	28
Food grains	21	17	13
Seeds	11	6	8
Tea	6	8	7
Hides and Skins	5	5	2
Other articles	17	18	16
	100	100	100

§ 9. The Direction of India's Trade:—The sub-joined tables show the percentage shares of foreign countries in India's total trade:—(Table A on this page and Table B on the next.)

Table A—Imports.

Name of the Country	1913-14	1918-19	1922-23	1926-27
United Kingdom	64.1	45.5	60.2	47.8
Germany	6.9	.....	5.1	7.3
Java	5.8	6.6	5.5	6.2
Japan	2.6	19.8	6.2	7.1
U. S. A.	2.6	9.5	5.7	7.9
Belgium	2.3	.80	2.7	2.9
Austria and Hungary (a)	2.3	.....	.1	.7
Straits Settlements	1.9	3.3	1.9	2.6
Persia, Arabia and Asiatic Turkey etc.	1.5			1.8
France	1.5	1.1	.8	1.5
Mauritius	1.4	1.5	.4	...
Italy	1.2	.5	.9	2.7
China	.9	1.4	1.2	1.4
Netherlands	.8	.1	.9	2.0
Australia	.5	1.3	.4	.7
Hongkong	.5	1.0	.6	.4
Ceylon	.4	1.7	.6	.6
Switzerland	.3			.9
East Africa and Zanzibar	.3			1.0

(a) Figures prior to 1922-23 represent Austria-Hungary.

These figures show that on the import side the United Kingdom, and Europe generally, dominate the situation, while a feature of the distribution of the export trade has always been the large number of countries participating in it, though the United Kingdom is still the biggest single customer for Indian exports. The causes of the predominance of the United Kingdom in India's trade have already been indicated, as also the successful attempts made by Germany and Japan to establish direct trade relations with India in the pre-War period, and by the United States during and since the War. We may now

Table B—*Exports.*

Name of the Country	1913-14	1918-19	1922-23	1926-27
United Kingdom	23.4	29.2	22.0	21.5
Germany	10.6		7.5	6.6
Japan	9.2	12.1	13.4	13.3
U. S. A.	8.9	13.8	11.5	11.1
France	7.1	3.6	5.1	4.5
Belgium	9.4	.004	3.8	2.9
Austria and Hungary	4.0	.06	.4	.1
Ceylon	3.7	4.2	4.1	4.8
Persia, Arabia, Asiatic Turkey etc.	3.2	4.0	3.4	2.6
Italy	3.2	2.2	2.2	3.7
Hongkong	3.2	2.9	2.5	1.0
Straits Settlements	2.8	1.1	4.6	3.1
China	2.3	.03		3.7
Netherlands	1.8	2.6	1.3	2.0
Australia	1.6		1.8	2.5
Russia	1.0		.003	.03
Spain	.8			.9
Java	.8	1.4	1.0	1.0
East Africa and Zanzibar	1.0			.6

(a) Figures prior to 1922-23 represent Austria-Hungary.

discuss the principal tendencies regarding the direction of India's trade as revealed by the above figures, during, before and after the War.

§ 10. Pre-War Distribution of India's Trade:—During the pre-War period there was a tendency for both the import and export trade to be diverted from the United Kingdom to other countries. As regards the distribution of imports, the United Kingdom supplied at the close of the last century as much as 69 per cent of the Indian imports. The share of Germany was only 2.4 per cent and that of U. S. A. 1.7 per cent., Japan being nowhere with its 0.6 per cent. By 1913-14 we notice that a remarkable change has taken place. While the share of the United Kingdom has come down to 64.1 per cent the German

share has increased to 6.9 per cent and of Japan and U. S. A. to 2.6 per cent each. Thus Germany occupied the second place next to the United Kingdom in 1913-14. The increase in the trade with Germany was attributed partly to the special technical skill which she had developed in certain lines and partly to the displacement of the expensive British goods by cheaper substitutes more readily absorbed by the Indian bazaars, and to the careful study which the Germans devoted to the needs and tastes of Indian customers. The share of Belgium, which supplied 3.9 per cent of the imports in 1903-04 was reduced to 2.3 per cent, while Java on account of her increased exports of sugar to India shot ahead and occupied the third place contributing 5.8 per cent of the total imports in 1913-14.

The export trade showed a similar tendency towards diversion from the United Kingdom in the pre-War period. At the beginning of the present century, roughly speaking 29 per cent of the exports went to the United Kingdom, 24 per cent to the Far East and 7 per cent to U. S. A. and the remaining 15 per cent to other countries. By 1914, the United Kingdom's share was reduced to 24 per cent, that of continental Europe rose to 29 per cent, the Far East took only 17 per cent owing to the fall in the exports of opium and yarn and the share of the United States rose to 9 per cent, and that of other countries to 21 per cent. It will thus be seen that during this period continental Europe gained what the United Kingdom lost. The loss in the Eastern market was made good by the gain in those of other minor countries. Turning to individual countries we find that, apart from the United Kingdom which was the biggest individual buyer of Indian goods, Germany which was third in the list in 1900 rose to the second place in 1914, the value of exports to Germany rising from £ 5.0 in 1900 to £ 17.5 millions in 1914, Japan showed a similar improvement in her buying capacity, her imports rising from £ 4.2 in 1900 to £ 15.1 millions in 1914. She thus advanced from the sixth place to the third as a buyer of Indian goods. China, on the other hand, lost the second place which she had occupied in 1900 and ranked sixth in 1914.*

* See R. M. Joshi: *op. cit.* pp. 159-160.

During the War period while the pre-War tendency of the import trade to move away from the United Kingdom gained further in strength, the United Kingdom lost further ground in the Indian market owing to her preoccupation with the War; the control of the Home Government on her exports and the restrictive effects of high prices. And her share in the import trade came down from 64.1 per cent in 1913-14 to 45.5 per cent in 1918-19. This, coupled with Germany's exit from the Indian market, created a gap in the import trade, a portion of which was rapidly filled up by Japan and the United States. Iron and steel and hardware previously supplied by the United Kingdom had now to be imported from these countries, while glassware, cotton piece-goods, paper etc, had to be imported from Japan and dye-stuffs from the United States. Both these countries made special efforts to study the requirements of the Indian market as Germany had done in the pre-War period and extended their commercial organisation in the country, which in the case of Japan included the establishment of retail stores in the principal Indian towns. The Japanese Exchange Banks in India also extended special financial facilities to the importers.*

On the export side, the tendency was for a temporary reversion of the trade to the United Kingdom and the British Empire as a result of the War-time purchases and special measures taken to facilitate them including restrictions on trade with neutral countries and the grant of credit facilities to some of the Dominions. All this was reflected in an increase in the share of the United Kingdom in the export trade from 23.4 per cent in 1913-14 to 29.2 per cent in 1918-19, while the share of the British

* "The most remarkable feature of the Japanese organisation for the development of foreign trade was the way in which all the branches of her commercial activity, the mercantile houses, the banks and the shipping companies, assisted by the Japanese Government, combined closely for the furtherance of the national interest, and, by means of the preferential treatment of their own people as against foreign competitors, managed to secure business for each other and to keep it out of the hands of their foreign rivals. This cohesion of all the interests for the furtherance of the national welfare was carried to an extent which was not achieved by any other nation, not even by commercial Germany before the war." Panandikar: op. cit. p. 84.

Empire as a whole increased from the pre-War average of 41.1 per cent to 51.7 per cent (War average). Germany of course disappeared altogether as a buyer from the Indian market. The shares of France and Belgium were also reduced on account of the occupation of their territories by Germany. Japan and the United States, on the other hand, increased their share from 9.2 per cent and 8.9 per cent in 1913-14 to 12.1 and 13.8 per cent respectively in 1918-19. This increase was due to several factors such as the privileged position held by these two countries as allies who, moreover, were removed far away from the theatres of the War, their increased export trade with India establishing credits for them and the conscious efforts made by both to develop direct trading relations with India. There was also a general reduction in the demand for Indian produce for normal industrial activity elsewhere. Thus, on the whole, during the war period India had to sell her produce in a restricted market and though she received higher prices for it than before the War, the prices she had to pay for her imports were far higher.

§ 11. Post-War Tendencies of India's Foreign Trade:—After a temporary and partial recovery on the import side in the early post-War period, the United Kingdom again experienced a set-back and the progressive decrease in her share in the import trade was accentuated in 1926-27 by the prolonged coal strike which seriously affected her industries, her share decreasing to 47.8 per cent of the total import trade in that year. The United Kingdom had once more to experience the competition of foreign countries such as Germany, Japan, United States etc. in the Indian market. We have already referred to the Japanese competition in cotton piecegoods in the Indian market not only with mills in India but also to some extent with Lancashire. Another explanation of the set-back to the import trade of Great Britain with India may be found in the fact that Great Britain buys much less from, than she sells to, India, whereas Japan, Germany and United States usually buy more heavily from India and thus are enabled to sell much. Japan and the United States have naturally lost part of the ground captured by them during the War, Japan receiving a special set-back owing to the commercial crisis of 1920-21. Another cause which has affected the

imports from both countries may be traced to the reappearance of old rivals and the restoration of more normal conditions of competition in the Indian markets. Germany has shown a remarkable recovery in recent years contributing 7.3 per cent of the total imports. She has gained from the industrial troubles in Great Britain to some extent and her percentage share in imports has even exceeded her share in the pre-War year 1913-14, which was 6.9. On the export side there is a definite tendency towards diversion, as was to be expected after the War, away from the United Kingdom, which diminished its share to 21.5 per cent. in 1926-27. Japan and the United States hold the second and third place respectively accounting for 13.3 per cent and 11.1 per cent of the total export trade in 1926-27. Germany has increased her share from 4 per cent in 1920 to 7 per cent. in 1925-26 and is soon likely to regain her pre-War position of importance as a buyer of Indian commodities.

To sum up the general trend of the post-War developments of India's foreign trade the pre-War tendency of a diversion of both the export and the import trade from the United Kingdom is reasserting itself more forcibly than ever. Japan and the United States are the most formidable competitors of England in the Indian market. Germany has fully regained her former position in respect of imports and her share in the export trade of India is rapidly increasing. All these nations command an excellent commercial organisation for pushing their trade with India: and in this respect they have stolen a march over the United Kingdom, which is now awakening to the necessity of following in their footsteps.

From the point of view of Indian interests, it goes without saying that it is an advantage to India to be able to buy her requirements in the cheapest markets and sell her products in the dearest, and therefore the present distribution of her import and export trade among a large number of countries competing with each other for India's custom and produce, rather than the predominance of one or a few countries, is not to be deplored, *pace* Imperialism and Imperial Preference.

TABLE I. Imports (percentage)

Name of the country	Cotton mfs.		Sugar		Iron & Steel		Machinery		Hard-ware		Motor cars etc.		Railway plant		Mineral Oils		Paper	
	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27
Unitedkingdom	90.1	75.3	1.8	2.2	69.9	62.0	89.8	78.2	57.2	36.4	71.3	26.7	93.0	61.6	5.7	2.2	56.0	35.5
U. S. A.	.4	.8	...	...	2.6	5.7	3.3	10.2	9.7	14.0	15.1	35.3	...	6.4	56.1	60.8	...	...
Germany	2.1	.7	.1	5.8	14.5	7.4	5.6	6.9	18.2	31.2	...	...	3.0	8.5	...	...	17.0	16.1
Belgium	...	...	...	1.6	11.5	18.7	...	1.8	...	...	4.5	.4	.7	11.8	...	...	...	...
Japan	1.8	17.2	...	...	...	...	...	...	1.5	5.7	...	...	...	...	...	...	...	...
France	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Italy	1.5	1.3	...	...	...	...	...	...	...	...	4.5	3.3	...	...	...	...	...	...
Netherlands	1.6	2.0	...	...	...	...	...	...	...	...	...	7.9	...	...	...	...	...	...
Australia	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	7.8
Norway	...	...	...	...	...	...	...	...	...	...	...	...	2.9	7.3	...	...	...	...
Sweden	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	10.1
Canada	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	3.1	7.1
Borneo	...	...	...	...	...	...	...	...	...	...	...	25.3	...	...	...	...	...	...
Java	...	...	71.8	73.7	...	...	...	...	...	...	...	...	...	...	21.8	14.3	...	...
Mauritius	...	...	16.9	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Persia	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Percentage of total trade represented by countries shown	97.5	97.3	90.6	83.3	98.5	93.8	98.7	97.1	86.6	87.3	95.4	98.9	99.6	95.6	87.3	92.1	83.6	76.6
Total value of trade (Rs. crores)	66.3	65.0	14.9	19.1	16.0	16.7	7.7	13.6	3.9	5.0	1.5	5.0	1.0	3.2	4.1	8.8	1.5	3.0

TABLE II. Exports (percentage).

Name of the country.	Tea		Jute		Jute mfs.		Cotton (raw)		Oil seeds		Food grains		Hides raw&tan,	
	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27	1913-14	1926-27
United Kingdom	72.4	85.0	38.0	22.9	6.3	5.4	3.5	2.6	22.2	13.5	26.7	9.4	25.9	46.6
Canada	4.3	2.9	...	...	...	...	...	...	...	...	...	...	...	...
Australia	3.1	1.9	...	...	10.6	11.7	...	...	...	...	...	...	...	...
U. S. A.	.7	2.1	11.9	12.0	41.5	35.0	...	...	...	...	...	...	...	...
Germany	...	...	21.8	27.6	...	...	14.6	4.1	16.0	15.3	7.8	7.6	24.3	25.3
Japan	...	...	...	...	.5	2.5	47.2	58.7	...	...	3.8	5.0	20.3	8.7
France	...	...	9.9	13.0	...	...	...	...	31.4	26.9	...	...	...	...
Italy	...	...	5.5	6.4	...	...	7.7	8.8	5.0	16.1	...	...	...	...
Belgium	...	...	.5	6.3	...	...	10.3	4.8	16.0	4.0	...	...	5.3	3.8
Ceylon	1.6	1.1	...	...	...	...	...	...	...	...	11.5	19.4	...	...
Russia	11.1	...	...	...	...	...	...	...	...	...	...	...	...	...
Persia etc.	1.2	2.7	...	...	...	...	...	...	...	...	...	...	...	...
Java	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Argentine Republic	...	...	...	...	2.5	3.3	...	...	...	...	...	...	...	...
*China	...	...	...	...	10.4	12.1	1.7	13.1	...	...	...	...	...	...
Spain	...	...	...	...	...	...	...	...	...	...	...	...	2.8	2.0
Netherlands	...	...	...	...	...	...	...	...	1.0	13.0	...	...	3.3	1.9
Straits Settlements	...	...	...	...	...	...	...	...	...	...	6.7	8.7	...	...
Percentage of total trade represented by countries shown	94.4	95.7	87.6	88.2	71.8	70.0	85.0	92.1	91.6	88.8	56.5	50.1	81.9	88.3
Total value of trade (Rs. crores)	14.9	29.0	30.8	26.7	28.2	53.1	41.0	58.6	25.6	19.0	45.1	39.2	15.9	14.5

* China includes Hongkong and Macao.

The tables on pages 290 and 291 above indicate the direction and variations of India's trade in some of the more important commodities. The main features regarding the direction of India's trade, most of which are clearly revealed by these tables, may be thus summed up:—

(a) *Imports*:—Though the United Kingdom is still the principal supplier of cotton manufactures to India, her share is steadily decreasing and that of Japan is increasing, especially in respect of cotton twist and yarn, and gray and coloured goods. Java dominates the imports of sugar, though her share fell from 87.5 of the total imports of sugar in 1925-26 to 73.7 per cent in 1926-27 owing to the competition of beet-producing countries. The United Kingdom is losing ground in the supply of iron and steel, machinery and hardware to U. S. A., Germany, Belgium, and even Japan, though she is still the largest single supplier, especially of iron and steel, and machinery. A similar tendency of diversion from the United Kingdom is in evidence regarding the imports of railway plant. As regards the imports of mineral oils, U.S.A. is still the principal supplier, Persia following her at a distance which is showing a tendency to decrease. As regards the imports of motor cars, U. S. A. Canada and France are rapidly gaining ground at the cost of the United Kingdom, though the British light car is steadily growing in popularity in the Indian market. Lastly, the imports of paper from Germany and Norway are showing a tendency to displace imports from the United Kingdom.

(b) *Exports*:—On the export side, the United Kingdom is by far the largest single customer for Indian tea, taking nearly 85 per cent of the total exports. But the United States is showing a steadily growing preference for Indian tea. Direct trade in tea with Russia is now insignificant, though she absorbed 11 per cent of the total exports of tea in the pre-War year. In raw jute, while the United States, Germany and the rest of Europe have more than regained the pre-War level, the takings of the United Kingdom are far below her pre-War standard of consumption. Germany is now the best customer for the Indian raw jute accounting for 27.6 per cent of the total export in 1926-27.

France, Belgium and Italy are other substantial customers for raw jute. In manufactured jute, the United States is the heaviest buyer owing to her large agricultural requirements, and absorbed 65 per cent of the exports of gunny cloth. Australia was the best market for sacking and gunny bags in 1926-27. The Argentine Republic, Java and Japan are other countries to which exports of jute manufactures are sent. In raw cotton Japan is the heaviest buyer and took 58.7 per cent of the total exports in 1926-27. China follows her at a respectable distance. The exports to these two countries are steadily on the increase owing to their growing cotton mill industry. On the other hand, exports of raw cotton to the continent of Europe and the United Kingdom have decreased. The biggest customer in Europe for Indian cotton is Italy, as Indian cotton is largely used there for the manufacture of cheap coloured cloth. In food grains, Ceylon is the best customer for Indian rice. The United Kingdom, Straits Settlements, Germany and Belgium are other large customers for Indian food grains. In oilseeds, France takes more ground-nut than any other country from India. The United Kingdom, Germany, Italy, Netherlands are other principal countries who import oilseeds from India. In hides and skins the United Kingdom and United States are the largest buyers. Germany has considerably reduced her share in the takings of raw hides as compared to her pre-war requirements, when she was one of the best purchasers of Indian hides. Italy also imports less than she used to. We have already mentioned that the increased consumption of meat on the Continent has considerably increased the supplies of domestic hides at prices so low that there is little inducement for the hides available in India to be brought down from the interior to the ports for export.

§ 12. Entrepot (Re-Exports) Trade of India :—The entrepot trade of a country consists of the re-exports of articles previously imported, the country in question serving merely as a convenient distributing centre. From very early times India has always had a certain amount of entrepot trade by reason principally of her geographical situation. Being situated in the centre of the Eastern hemisphere she is a convenient halting place for the trade between the Far East and the West. Thus in the old

times, "This section of our trade consisted chiefly of the import of silk-goods and porcelain from China, pearls from Ceylon precious stones and spices from the islands of the Eastern Archipelago—all for purposes of re-export to countries of the West; Venetian glass and the like from countries of the West to be re-exported to the East."* In more recent times India's entrepot trade was seen steadily to expand till a short while ago showing an increase from Rs. 5.80 crores in 1882-83 to Rs. 18.04 crores in 1920-21. Since the latter year however, it has fallen, and amounted to Rs. 13½ crores in 1924-25, Rs. 10½ crores in 1925-26 and Rs 8 crores in 1926-27. The fall in the last year mentioned was due to a decrease under the head of sugar, raw cotton, piecegoods, spices, leather, etc. The percentage shares of the principal countries in the re-export of India in the same year were as follows:—United Kingdom 36 per cent, U. S. A. 9 per cent, Persia 8 per cent, Ceylon and Mesopotamia 5 per cent each, Japan 3 per cent, and Straits Settlement 2 per cent. Other countries participating in India's re-export trade were Egypt, Kenya, Mauritius Portugese East Africa, Zanzibar, etc. in Africa; and Aden, Arabia, Hongkong, Asiatic Turkey, etc. in Asia.

The following table shows the value of the principal articles of foreign merchandise re-exported from India in 1916-17 and 1925-26:—

(In thousands of Rupees)

Articles	1916-1917	1925-26	Articles	1916-17	1925-26
Apparel	10,32	21,67	Metals	35,81	19,31
Cotton manufactures	2,67,05	1,48,49	Provisions	22,31	4,93
„ Twist & Yarn	13,23	13,95	Spices	9,49	20,20
Fruits and vegetables	52,78	17,26	Sugar	89,63	50,64
Hardware	13,35	25,76	Wool raw	1,03,97	90,36
Gums and Resins	16,19	16,06	Other articles	1,77,71	6,19,85
Total				8,11,84	10,48,48.

* K. T. Shah: op. cit., p. 92.

It will be seen from the above table that the re-export trade is mainly in manufactured articles imported from Western countries, especially cotton textiles which are taken by Persia, Muscat, and East Africa. The principal article re-exported to Western countries is raw wool which is imported across the land frontiers of India, the bulk of which goes to the United Kingdom. A certain amount of fur skins from Persia are exported from Bombay, which also re-exports pearls previously imported from Bahrein Islands, Muscat. etc.

Though India will always act as a distributing centre to a certain extent particularly for those of the Asiatic countries who have no sea-board of their own and to whom the Indian ports are the nearest approach for maintaining trade relations with other countries, the prospects of the entrepot trade of India do not seem to be altogether bright in view of the growing tendency towards the establishment of direct trade relations among the various countries lessening their dependence on India as an entrepot. The fall in the value and quantity of the re-export trade in the last few years seems to bear this out.

§ 13. Balance of Trade and Balance of Accounts:--A chronic and much noticed feature of India's foreign trade is the excess of exports of merchandise over imports. Occasionally India has experienced what is called an adverse balance of trade, that is to say, there has been an excess of imports of merchandise over exports, e. g. in the year 1920-21 and again in 1921-1922. But this is very much the exception rather than the rule, the normal state of affairs being a favourable balance of trade. Part of this balance is liquidated by the net imports of treasure. (i. e. imports of treasure *minus* the exports of treasure). But even then a large amount of the excess of exports remains to be accounted for as seen from the following table, which gives statistics relating to (a) net exports of merchandise; (b) net imports of treasure, i. e., imports of treasure, *minus* exports of treasure; and (c) net exports of total trade, i. e., net exports of merchandise *minus* net imports of treasure* :

* S. C. Bose: *The Foreign Trade of India*, M. A. Thesis (unpublished).

(Value in lakhs of Rupees)

Year	Net exports of merchan- dise	Net imports of treasure	Net exports of total trade
1840-41	5,04	1,42	3,62
1850-51	6,60	3,27	3,33
1860-61	9,48	9,56	, -8
1870-71	20,87	3,22	17,65
1880-81	21,47	7,55	13,92
1889-90	34,26	15,56	18,70
‡1900-01	16,83	10,45	6,38
1910-11	76,26	32,61	43,65
1913-14	57,70	36,36	21,34
1917-18	80,55	44,22	36,33
1919-20	1,14,32	64,56	49,76
1920-21	- 79,81	8,59	-88,40
1921-22	- 33,94	12,23	-46,17
1922-23	69,88	60,56	9,32
1923-24	1,26,19	49,93	76,66
1924-25	1,46,88	94,03	52,85
1925-26	1,50,81	81,65	99,16
1926-27	71,13	39,32	31,81

(Re-exports and transactions on Government account are included.)

This table leaves no doubt as regards the excess of exports over imports as a tendency, which on the whole seems to be getting more and more pronounced.

In a proper balance of accounts, however, there must be an exact equivalence between exports and imports, and this will be seen to be established, if we could take into account not only the visible items, that is to say, those items which are recorded in the customs returns or in other published statistics, but also those items which are not thus recorded.

§ 14 Credit and Debit Items in India's Balance Sheet:—We shall now consider what items have to be taken into account for a complete international balance sheet and how India stands with regard to each of them:— *

* See Morison : *The Economic Transition in India*, Chap VIII

‡ Famine year.

1. Imports and exports of merchandise :—Under this head, as we have already seen, India is a creditor country. (2) With regard to treasure, however, India imports more than she exports and therefore she is a debtor on this account. (2) Loans offered or received from abroad :—While a loan is being carried out, the nation which contracts the debt is the creditor and the nation which advances the loan is the debtor. Under this head India is a creditor country as she has to raise large loans in England from time to time. (3) The annual interest on capital already invested has the opposite effect making the borrowing country a debtor and the lending country the creditor, and as India has to make annual remittances of interest on the loans she has contracted she is debtor under this head. (4) The repayment of the loan itself also makes the borrowing country the debtor and the lending country the creditor. And as India is constantly paying off portions of her foreign debt in addition to paying the interest year after year, she is under this head a debtor country. The repayment of the loan may take the form of Indians purchasing the Rupee Paper held in England and thus bringing the debt home. But the effect of this is the same as if the Government had paid the debt out of its revenues viz. that India's foreign obligations are lessened so far. (5) The earnings of Indians living abroad and of foreigners residing in India so far as they are remitted in each case to their native country by the parties concerned:—In the former case India is a creditor and in the latter she is a debtor. But on the whole, under this head India is a debtor. The remittances abroad of European merchants and businessmen, bankers and Government Officials far outweigh the remittances to this country of Indian merchants and coolies residing outside India. (6) The profits of foreign banks and shipping and insurance companies:—India's payments under the head of banking profits, shipping freights and premiums of insurance, are not precisely calculated but must aggregate to a very large sum representing India's indebtedness to that extent. (7) The remittances of money by foreigners for benevolent purposes to a country or donations sent abroad by the country make

it a creditor in the former case and a debtor in the latter. Under this head India is a creditor country, because she receives more money from Europe and America for the support of missions and missionary schools in India as well as in the form of occasional subscriptions, raised abroad for the relief of famines in India and other calamities, than she sends to foreign countries for similar purposes. (8) The expenditure of a nation's Government abroad will make it a debtor to that extent, and conversely the expenditure of other governments in a country will make it so far a creditor. On this account India is a debtor as she has to spend large amounts of money in England by way of furlough pay and pensions of European officers who have served in India and for the purchase of stores etc. She has also to pay the English Government for various kinds of expenditure incurred by the latter for India. All this expenditure on government account in England is included under the Home Charges. (9) The payment of tributes or indemnities obviously makes the paying country debtor and the receiving country creditor. As India neither pays nor receives a tribute or indemnity, this heading has to be altogether ignored. (10) The expenditure of foreign tourists in India and Indian tourists abroad:— Under this head India is a creditor because the number of foreigners visiting India for sight-seeing is far greater than the number of Indians visiting foreign countries. (11) On the other hand, India is a debtor to the extent of the remittances for the education of Indian students abroad. The amount thus spent is somewhere in the neighbourhood of a crore of rupees every year, and there is every prospect of its increasing in the future.

For a complete balance sheet, therefore, we will have to reckon in all these items, and when that is done the two sides of the account must balance each other.

In the following statement on the right-hand side we have India's debit items i. e. those on account of which India has to pay more money abroad than she receives; and on the left-hand side, we have the credit items i. e. those on account of which more money is owing to India *from* foreign countries than she owes *to* foreign countries:—

<i>Credit</i>	<i>Debit</i>
1. Exports of merchandise.	1. Imports of treasure.
2. Loans raised abroad.	2. Interest on loans raised abroad.
3. Remittances by foreigners to India for the support of schools and missions and for the relief of famines and other charitable purposes.	3. Repayments of loans previously incurred.
4. Tourists' expenses.	4. Remittances abroad by European merchants, lawyers, Government officers, etc.
	5. Profits of foreign banks and insurance companies and freight charges paid to foreign shipping companies.
	6. Expenditure on Government account abroad in connection with furlough pay, pensions and stores and bullion etc. purchased for the Government of India. (Home charges.)
	7. Remittances to Indian students abroad.

§ 15, India's visible balance of account:—In the table on p. 296 we saw exhibited in the last column a large and growing excess of exports over imports. That table, however takes notice only of merchandise and treasure; whereas the following statement,* although it excludes government stores and government treasure, goes a few steps further towards the construction of a complete balance of accounts by including the transfer of funds from and to India through Government.

The statement gives India's visible balance of accounts for 1926-27. The detailed figures work up to a *plus* or *minus* balance

* Taken from the Report of the Controller of the Currency for 1926-27

(plus representing net export and minus representing net import) for each of the three main heads of classification, namely, (1) private imports and exports of merchandise, (2) private imports and exports of treasure, and (3) remittance through Government—all leading up to a *plus* or *minus* total (in this case plus) for the transactions as a whole. (In lakhs of Rupees)

	1926-27
Exports of Indian merchandise.(Private)	+ 3,01,45
Re-exports of foreign merchandise (private)	+ 8,01
Imports of foreign merchandise (private)	-2,30,17
<i>Balance of Trade in merchandise (private)</i>	+ 79,29
Gold (private)	-19,40
Silver (private)	-19,79
Currency notes (private)	-14
Balance of transactions in treasure (private)	-39,33
<i>Total visible balance of trade</i>	+ 39,96
Council bills and telegraphic transfers paid in India, purchases of sterling from banks and firms in India and payments for sterling taken over London from local bodies.	-2,82
Sterling transfers on London sold in India	+ 1,93
Transfers of Government Securities	+ 3
Interest drafts on India in respect of Government of India securities	-34
<i>Balance of remittance of funds.</i>	-1,20
<i>Total visible balance of accounts.</i>	+ 38,76

The balance (38, 76 lakhs of Rupees) finally left here must be taken to represent the net effect of the remaining items, for any one of which we have no precisely calculated or recorded figure.

§ 16, The 'Drain' defined :—India's habitual excess of exports over imports has given rise to the 'Drain' theory, which, whatever its other vagaries, has at least served to educate the people of India out of a very common mercantilist fallacy. That fallacy is that a favourable trade balance or excess of exports over imports is necessarily a good thing, just as an excess of imports is necessarily an evil thing. This excess of exports

has been looked upon by many people as a measure of the tribute paid by India to England owing to her political subjection. For all the outgoings represented by this excess of exports, India of course receives some kind of return, and they can all be accounted for more or less accurately, as we have already seen. But as the Spanish proverb says, "the accounts are all right but the treasury is empty." The real point is not whether *some* kind of equivalent is received, but whether the return is in every way adequate.

Sir Theodore Morison defines the "drain" as that portion India's debits for which in any given year she receives no material equivalent in goods or money. He, however, forestalls an objection to this definition to the effect that, in any given year the excess of exports may appear less than it actually is, because a foreign loan may have been contracted and received in the form of imports of various kinds, and this would reduce to that extent the real excess of exports to be accounted for and justified. The loan will have to be repaid in subsequent years and will then cause an increase in exports and in the amount of the 'drain,' and therefore does not represent a real gain. In order to meet this objection, Sir Theodore Morison takes the "drain" to mean potential drain, that is to say, that portion of India's debits, as they would have been in the absence of foreign loans, for which in any given year she receives no material equivalent. However, we prefer to adopt the first of these definitions. Because we are less concerned with an accurate appraisement of the *amount* of the 'drain' than with a general discussion as to how far the various items accounting for it can be regarded as adequate returns, and as interest on debt is one of the most important of these items and raises important issues, it would be inadvisable to accept a definition which would compel us to leave it out of consideration.

§ 17. The Home Charges :—India's excess of exports over imports is largely accounted for by the Home Charges.

* The following figures show the great growth of the Home Charges during the last sixty-five years or so :—

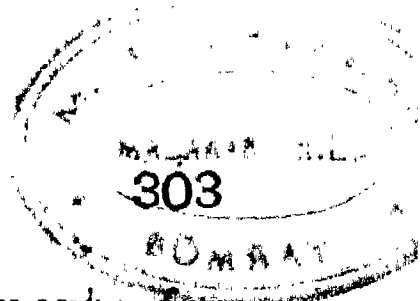
* See Shah, : *Sixty years of Indian Finance*, pp. 187-188

Gross Sterling Expenditure in England (In £)

Year	Amount	Year	Amount	Year	Amount
1859-60	5,042,945	1899-1900	16,392,864	1922-23	31,744,737
1869-70	7,677,850	1909-10	19,122,916	1923-24	34,156,480
1879-80	14,543,277	1913-14	20,311,673	1924-25	30,093,456
1889-90	14,848,923	1918-19	23,629,495	1925-26	29,969,999

The principal items of expenditure (charged against revenue and receipts in England in sterling) included in the Home Charges are as given below :—

<i>Expenditure (1926-27)</i>	Central & Provincial (£.)
1. Interest on debt (other than that charged to Railways and Irrigation Works) and on other obligations	5,809,8. 5
2. State Railways (Interest, Annuities and Sinking Funds)	8,539,450
3. Charges on account of Departments in India such as Post and. Telegraph, Political, Mint, etc.	2,109 267
4. Public Works (Furlough, Absentee Allowances, etc.)	371,090
5. *Military Charges	8,081,706
6. Marine	168,851
7. Civil Charges (Establishment of the India Office and of the High Commissioner for India etc.	240,414
8. Pensions and Allowances	2,132,592
9. Stores for India	2,368,893
10. Miscellaneous charges	148,161
Total ...	29,969,999
<i>Receipts.</i>	
Receipts (such as Military receipts, Receipts of Interest etc.)	4,615,736
Net Expenditure in England	25,354,263



(*Military charges include effective charges payments for British forces furlough allowances, troops service and passage money etc., and non-effective charges, such as payments in connection with retired pay, pensions, etc of British forces and pay and pensions of non-effective and retired Indian officers).

We will exclude from consideration the payment on account of stores purchased on behalf of India in England, because the stores are a material equivalent and figure in the returns for imports. We have already seen that it is an arguable point whether these purchases of government stores could not be effected more cheaply and whether a larger reliance on the Indian market for their supply is not feasible. But in the 'drain' controversy what we are concerned with is the immaterial and not the material equivalents.

§ 18 Payments in connection with foreign loans:—One of the most important items in the Home Charges is interest on debt which has arisen in consequence of government borrowings in England for financing railways, irrigation works etc. The various questions relating to the employment of foreign capital in this country have already been discussed,^{\$} and it should no longer be necessary to emphasise at this stage that borrowing money from abroad is not necessarily an evil, but that, on the contrary, foreign loans are often to be regarded as highly satisfactory incidents of economic development. Many countries which are rich in national resources but poor in capital find it necessary and profitable to borrow from other countries, and some of the debtor countries like Canada are among the most prosperous in the world and getting more and more prosperous with the help of foreign capital. It is obviously absurd to describe the interest on these loans as a 'drain,' and since it is the interest on foreign debt that figures most prominently in the Home Charges as well as in the rest of India's disbursements abroad, Sir Theodore Morison proposes to substitute the colourless expression, "foreign

* The above table has been compiled from detailed figures given in the Statistical Abstract for British India for 1925-26 pp. 156-159, to which the reader should refer for further details regarding the Home Charges.

\$ See Vol I, Chap XIII.

payments " or ' net foreign payments ' instead of the misleading word ' drain,' which suggests that these payments are harmful to the country. He argues that this part of India's indebtedness at any rate cannot be regarded as a drain on the country's resources caused by her political connection with England. For even if she were outside the Empire it would have been necessary for her to raise these loans for the purpose of developing her resources. The fact that these debts are incurred in England has nothing whatever to do with India's political subjection to England. The debts are raised in London because London happens to be the cheapest money market in the world. It is further contended that the political connection with England, far from being a handicap to India, is of distinct advantage to her in this respect, because it has raised India's credit abroad and has enabled her to borrow on more advantageous terms than would have been possible otherwise. It is true that the English Government does not directly guarantee India's credit, but the British Government in India has, by ensuring a stable administration and by promoting the economic development of the country, improved her credit abroad. India is thus able to raise foreign loans at perceptibly lower rates than a number of other countries like Japan, and this is a continually increasing advantage, because, for a long time to come, India would have to borrow capital on a large scale, in order to be able to proceed satisfactorily with the task of industrialisation on which she has set her heart, and even if she is able to obtain an advantage of no more than one per cent on the rate of interest, she would make a clear saving of one million pounds on every hundred million pounds that she borrows. The statement, however, that India has been able to borrow more cheaply than other countries has been challenged, and it is pointed out that even the South American Republics have not been at an appreciable disadvantage in this respect. But whether this is so or not, the discussion of the question as to what English credit has achieved for India brings us dangerously on the brink of the fascinating but futile controversy as to whether, after the downfall of the Moghul Empire, India would have been able to evolve a stable form of Government without the assistance of Great Britain, and whe-

ther she would have been able to obtain loans on terms not very different from those at which she borrows at present. We must, however, decline to be drawn into such hypothetical arguments and limit ourselves as far as possible to what is rather than to what might have been. Leaving aside, therefore, the question whether an independent India would have been able to attract capital investments from abroad in the same way as at present, what we are called upon to declare in the present discussion is whether, with better management, the burden of the debt, both as regards principal and interest, could not have been appreciably reduced. In this connection we shall restrict ourselves to the consideration of the most representative as well as the most important of our borrowings, viz., those for railway construction in this country. The various issues that would be relevant are whether all the railways that have been built were required in the best interests of the country, and whether in some cases the need for transport facilities could not have been met more cheaply by other modes of transport such as roads and canals; whether to some extent the expenditure on railways was not at the sacrifice of other more deserving claimants for public funds like irrigation works; whether the inducements offered to foreign capital in the shape of guaranteed rates of interest were not excessive; and whether the railway system was worked as efficiently and cheaply as possible with a consistent regard for national interests. All these questions have already been discussed and we need merely repeat here that, in all these respects mistakes have been committed, and so far our payments in connection with these loans cannot be said to be compensated fully by economic equivalents. If it is claimed that the railways have been on the whole "the harbingers of economic prosperity" in India and that the actual advantages, direct as well as indirect, more than outweigh the cost of the construction we need not dispute this claim. But the real point at issue is whether these great benefits from railways have not been secured at a needlessly heavy cost.

Payment in the form of interest and profits on the foreign capital which has sought investment in this country without

government intervention and mediation do not appear under the Home Charges, but they account for a substantial portion of our excess of exports. Here again, the question resolves itself into a discussion of the advantages and disadvantages of foreign capital in India and we can only refer the reader to the relevant sections (§13 onwards) in chapter XIII Vol. I, where this subject has been treated. We had there occasion to note that along with some great and undoubted advantages, certain serious disadvantages have resulted from the unrestricted admission of foreign capital and therefore, the statement that "India illustrates in its most obvious form the advantage of borrowing foreign capital,"* cannot be accepted without reservation. But whatever the disadvantages of foreign capital, they can be connected, if at all, only indirectly with India's political subjection to England, and this applies generally to all the items in the 'drain' that do not appear under the Home Charges e. g. freight charges, profits of shipping and insurance companies etc. noticed below in § 19.

§ 18. Civil and Military Services:—We now come to that part of our payments which is made in respect of civil and military services. Here the question whether we get an adequate return for our payments will depend upon the manner in which we answer the following questions. Is the European agency employed in this country, indispensable and if so to what extent? Whether the salaries that are at present deemed to be necessary to attract the requisite type of European in the various branches of public service are not too high, and whether the process of Indianisation has gone as far as it might without endangering efficiency or bringing in its train other serious disadvantages? All these questions will be answered differently by different people. But there is a general feeling that on all these accounts India's expenditure is higher than it might be. It may be true that India has at present "an administration more favourable to economic evolution than she could provide herself."† But even the most moderate of Indian politicians will not admit that there is no scope for further economy or Indianization. The demand for the substitution

* Morison : *The Economic Transition in India*, p. 218.

† Ibid p. 241.

of an Indian for a European agency wherever possible is not based merely on the ground of its relative cheapness. There are other considerations which are equally important. For example, there is the consideration that the experience of the Indian officer, unlike that of the European officer, is not lost to the country on his retirement. Further, the relative inferiority of the Indian, wherever it must be taken as established, can in many cases be accounted for by the lack of adequate opportunity given to the Indian so far. What is more important than anything else, however, is that it is the Indian's birth-right to be preferred in civil and military employment in his own country, even where he is slightly inferior to the European, and much more so when he is quite as fit.

In connection with the military charges another question apart from that of Indianisation is whether the strength of the army at present maintained in India is not above her proper requirements. The non-official opinion is that the army is bigger than is required for purposes of Indian defence. On the other side, however, it is contended that, even supposing the expenditure on the army in India is larger than it need be from the purely Indian point of view, India is on the whole a gainer. For she contributes only a small sum towards the upkeep of the British Navy, whose services are indispensable for protecting her from invasion. If India were called upon to look after her own naval defence, she would have to spend a very much larger amount on her navy. But on the other hand, it must be remembered that the British Navy is not maintained entirely for the purpose of guarding India's shores from invasion. Australia, for example, benefits perhaps even more than India from the British Navy, though her present contribution towards it is far from commensurate with the advantage enjoyed by her. Nor is she asked to maintain an army of a strength beyond her actual requirements for Imperial uses. The principle according to which the strength of the Indian army ought to be determined is that of making it just adequate for the defence of the country, and this furnishes the only test to be applied in deciding whether the military expenditure of India so far as it

is due to the size of the army alone is excessive or not. It is indeed unreasonable to expect that England should continue without complaint to bear the greater part of the expenditure on the navy whose services are available not only to herself but to every other part of the Empire, and in the future, proposals will probably be made in order to distribute expenditure amongst the different parts of the Empire so as to relieve England of the excessive burden of her responsibility in this connection. It would, however, be absurd to suggest that each of the constituent members of the Empire should contribute a sum representing the full benefit derived by it from the British navy. The capacity of each member to bear any additional burden would be a more reasonable criterion, and the comparative poverty of India would be a valid plea for a moderate charge being levied upon her. Even so, however, it is probable that her contribution would have to be more substantial than at present, and if matters are properly put to her, she will not and ought not to grudge this. But the whole question of the naval defence of the Empire requires to be treated separately on its own merits and should not be mixed up with the question as to whether the present military expenditure of India is not capable of being appreciably reduced. If the Indian Army is meant purely for the purpose of securing freedom for the country from external aggression and internal commotion, its size, personnel and organisation are matters which must be determined on other principles than if it is meant for Imperial purposes. The Assembly repudiated the suggestion underlying the Report of the Esher Committee of 1919 that the Indian Army is to be regarded as part of the total armed forces of the Empire. Actually, however, the army has been frequently used for Imperial purposes, and the contention that, if it is intended to persist in this policy, part of India's military expenditure should be borne by England, does not appear to be unreasonable.

§ 19. Profits of Bankers, and of Shipping and Insurance Companies:—Other services than those noticed above for which also India has to make a payment abroad and which are not exhibited under the Home Charges are those of foreign bankers, European shipping and insurance companies etc. It is one of the

cherished aspirations of the Indian people to be able before long to do much of this work for themselves. To say that this is a commendable ambition is not to forget the fact that even wealthy countries sometimes find it advantageous to buy such services from foreign nations. For example, the United States used to be largely indebted, at least before the War, to the principal European Powers for marine transport service, banking, insurance, and other financial and commercial services. But the plea that India should learn to rely on herself in these matters is based on the idea that, by so doing, she will certainly reap great economic and other advantages, while lessening the magnitude of the 'drain'.

§ 19. Some basic assumptions of the 'drain' controversy:—
As a set-off against the various losses incurred by India on account of the 'drain' it is sometimes urged that, after all, England has conferred on India the inestimable boon of peace and has made possible an orderly development of the country in all directions and that, therefore, her losses due to the 'drain' are as dust in the balance when weighed against these blessings. On this plan, however, it would be possible to justify every kind of Government extravagance and unfairness. A large number of thinking people in this country would readily admit the great advantages to India of the British connection. But precisely because they are immeasurable, no attempt should be made to measure them. They should not be dragged into a discussion which is occupied with more definite and calculable, though perhaps less fundamental, matters; just as we should also refuse to consider as a part of this controversy, the incalculable, though none the less real, advantages which England derives from India. We may be able to compute roughly the advantages which her businessmen derive from the scope which India offers for their activities and enterprise. But by what calculus shall we estimate the gain to England from the enormous increase in her international prestige due to her possession of India, or how shall we attempt to fix the value in terms of pounds, shillings and pence, of the glow of pride and power, which Englishmen feel when they contemplate this magnificent empire, or of the

value to England of India as an unrivalled field for the training of her soldiers, statesmen and administrators? The question of the drain, if it is going to lead to any useful conclusions, must leave out of consideration all these impalpable advantages.

As against those who are impressed with the great benefits, which British rule has conferred on India, there are others who feel that nothing can really be held to compensate for loss of political freedom. But those who are of this opinion have obviously no right to engage in a discussion of this kind. For, the 'drain,' theory seeks an answer to the question, how far the compensation which India obtains for the outgoings represented by the excess of exports is adequate, and in so framing the question admits the possibility of compensation. If arguments with reference to the infinite advantages of *Pax Britannica* are to be ruled out of court, so must arguments about the infinite degradation involved in the loss of liberty.

§ 20. Economics and Politics of the Drain Theory :—From the foregoing discussion it will have been clear that much of the 'drain theory' in its present form has come to be a somewhat diffused and not very effective criticism of British administration in India. Its association with political agitation and propaganda has been responsible for a good deal of unsound economics. One of the earlier crudities of the theory was to suppose that the annual drain was a tribute exacted by England from India in the form of actual treasure. This was, however, seen to be in flat contradiction with facts which showed a large net Indian import of gold and silver. The next stage was to assume that the whole of the excess of exports represented so much net loss to the country. This position was also abandoned and, as we have just seen, it is now usual to admit that some return is being received in the form of various kinds of services, though it is maintained by many people that India is required to pay too heavily for them. As a result of these successive modifications, the 'drain' theory has lost much of its original full-blooded character. The analysis undertaken in connection with it, however, still remains useful as indicating various injustices and directions of urgent reform. Nevertheless we are of opinion that the word 'drain' has been one of the most heavily worked in the whole phraseology of

Indian Economics, and, as hinted in our Preface, it has been invoked too often to explain everything that is "rotten in the state of Denmark." It has served to summarise all the woes and burning thoughts of at least two generations of patriots, and to many Indians of the generation of Dadabhai Naoroji, the use of the word 'drain' seems to have appeared singularly apt in view of a certain famous utterance of a rather cynical Secretary of State, who had a fatal facility for incisive language, and who talked of the necessity of "bleeding India."*

Economics in this country began by being an ally of politics and the drain theory was the first product of the association between the two. It suggested that the intense poverty of India was very largely, if not entirely, due to the tribute exacted by England from India. We have seen above how the 'drain' theory has been much improved of late by the introduction of many necessary qualifications and how it still points to the existence of a number of real grievances. It does not, however, furnish anything like a complete explanation of Indian poverty. The first Indian thinker to see the necessity of emphasising many other more important causes was Ranade, who was a path-breaker in this as in so many other matters.† Later writers have perhaps not always shown Ranade's insight and his exquisite sense of proportion.

§ 21, Land Frontier Trade:—India has an extensive land frontier (about 6000 miles) on the North-West and North-East, considerably exceeding her sea-coast in length. But at many points it offers great difficulties for commerce owing to obstacles such as dense and impenetrable forests and inaccessible mountains. There are only a few openings or passes like the Bolan Pass on the

* Lord Salisbury, Secretary of State for India, said in 1875, "As India must be bled, the lancet should be directed to the parts where the blood is congested, or at least is sufficient, not to those which are already feeble from the want of it." It was not so much the unusual frankness which characterised this utterance nor the idea it conveyed (which after all was not so very wicked when the whole context is considered) as the sanguinary language employed, that caused so much resentment in India and was responsible for the notoriety which it attained.

† Cf. D. A. Shah, *The Indian Point of View in Economics*, p. 12.

North-West frontier which make communication with trans-frontier countries possible. In our historical survey of India's foreign trade we have already drawn attention to the ancient character of the land frontier trade of India, which was fairly brisk during the Moghul period. In more recent times, the position in respect of trans-frontier communications has been considerably improved, especially on the North-West frontier. Though the principal motive in laying out the frontier railway was strategic, it is also serving as an artery of commerce. The principal trans-frontier countries with which India has trading connections are Afghanistan, Central Asia, Persia, Nepal, Tibet, Shan States, Western China, Siam etc. The course of the land frontier trade during the last few years is summed up in the following table:—

(In crores of Rupees)

	1916-17	1918-19	1920-21	1922-23	1925-26	1926-27
Imports	12.81	15.96	18.16	18.27	Discontinued from April 1925	
Exports	10.34	14.87	15.81	15.20		
Total land trade	23.15	30.84	33.97	33.48		

These figures, while they are insignificant in comparison with the total sea-borne trade of India of Rs. 600 crores and odd, yet reveal a steady progress, which is likely to be quicker with further improvements in trans-frontier communications. The principal commodities at present imported from the trans-frontier countries are food-stuffs such as wheat, grain, pulse and rice; fruits, vegetables and nuts especially from Afghanistan; raw wool from Afghanistan and Tibet; raw jute and oilseeds from Nepal, living animals, principally from Nepal; raw silk etc. By far the most important exports are cotton goods, foreign and Indian; cotton yarn; sugar, raw cotton, petroleum, leather manufactures, silk goods, tea, apparel etc.* Now that

* Statistical abstract 1925-26, pp. 536-537.

some of the neighbouring countries like Afghanistan are waking up from their age-long sleep and are pulsating with a new-born ambition to come into line with the advanced nations of the world, their progressive modernisation is bound to have a beneficial influence on our trans-frontier trade. It would be manifestly to the advantage of India to develop this branch of her external trade to the utmost possible extent, especially as, with the progress of the manufacturing industries in India, the importance of nursing trans-frontier markets will be greater than ever before.

§ 22. International Trade and Economic Prosperity:—The *aggregate* volume of India's trade, is sufficiently large to entitle her to the fifth place among the countries of the world in the following order, the United Kingdom, the United States, France, Germany and India. As regard *per capita* trade however India stands very nearly at the bottom as the following table shows:—

* Foreign Trade per head of population (Special trade in merchandise only).

(In U. S. A. Dollars.)

Country	1913	1921	1925
Australia	155	175	255
Canada	142	258	244
Denmark	134	233	233
United Kingdom	126	253	208
Belgium	209	212	192
France	74	130	105
Germany	74	48	80
United States	43	63	79
Japan	12	38	33
India	4.3	7.0	7.3
Russia	8.5	3.2	4.7
China	1.6	3.7	3.2

* League of Nations Memorandum on Foreign Trade Balances, Vol. I, p. 110, (quoted by Mr. S. C. Bose in his M. A. Thesis: *The Foreign Trade of India.*)

It is obvious that in the case of a large country like India with a huge population a very considerable increase in the volume of the total trade is required to show a given amount of growth per head than in the case of small countries.

The question how far the *per capita* foreign trade of a country is reliable as an index of its economic position is not easy to answer. It certainly cannot be taken as an infallible index of economic prosperity. For instance, if we were to take the *per capita* trade as a dependable criterion, we should conclude that the United Kingdom is considerably richer than the United States. But we know as a matter of fact that the true position is precisely the reverse of this. It would scarcely be an exaggeration to say that the very existence of the United Kingdom depends on a prosperous foreign trade, whereas to the United States her foreign trade is of slight importance as compared to her internal trade. And generally speaking it will be found that international exchange is of far greater importance to small than to big nations. However, the safest thing for the student is to remember that international trade is governed by the principle of comparative costs and not by the wealth or poverty of the countries engaging in it. The size of the aggregate—and to a smaller extent the *per capita*—income may sometimes serve to corroborate conclusions in regard to the relative economic strength of nations arrived at by the application of surer tests such as the *per capita* income; but there is much risk in making it the sole basis for such inferences. Dr. Marshall has treated the whole question in all its aspects with his usual fulness and ability, and we may be pardoned for quoting freely from him. Comparing India with the West Indies in the days before England had yet become the workshop of the world, he points out that “when natural and artificial causes were combining to give the West Indies nearly a monopoly of the production of sugar, some of these islands imported not only all their clothing and other manufactures, but also nearly all their food. On the other hand, India had at the time but little foreign trade, in spite of her vast population and the high value which Europe placed upon many of her products. For she had little need of European products; she could herself supply most of the things which she desired to have;

and Europeans could not get access to more than a narrow fringe of the large and rich land. Consequently while the foreign trade of the West Indies was for a time one of the largest in the world, that of the whole continent of India remained small." All the same, however, India was a wealthier country than the West Indies.* Dr. Marshall has also observed that "A country's foreign trade is likely to be increased by rapid advance in those industries which are already ahead of similar industries in other countries ; because such an advance increases her power of exporting at a profit. But her foreign trade is likely to be lessened; or at all events its growth is likely to be checked by an advance in those industries in which she is relatively weak, because such an advance will tend to diminish her need of exports." A large *per capita* foreign trade may "indicate that a nation is prosperous and enjoys comforts and luxuries by participating in an international exchange of commodities, or, on the other hand, it may indicate that the people live in a poor and unproductive territory and are compelled to give services and import bare necessities, articles of simple food, and clothing, fuel and building material and sometimes even drinking water, as in the case of Aden, in Southern Arabia." † At the same time, however, so far as actual experience goes, great national trade has almost invariably been an evidence of high industrial energy, especially when we are considering not so much a large *per capita* as a very large *aggregate*, external trade. "For, the same energy of character, that makes a nation eminent in industry, is likely to make her traders alert to seize every opportunity of bringing the products in which she excels, to the notice of countries that cannot produce those things with as much relative ease and efficiency as they can other products, which are in demand in her own market but cannot be produced there with as much ease. The case is specially strong when the exports consist largely of high grade products." A large aggregate trade commonly indicates high industrial efficiency. It shows that in the country in question, "each sort and degree of skill is set to the work for which it is specially adapted; plant

* Marshall : *Industry and Trade*, p. 25.

† *Ibid*, p. 14.

is improved rapidly; and that which is no longer the best of its kind is quickly thrown out often to be exported to countries whose industries are still backward."

In the light of the above considerations we may conclude that the great increase in India's foreign trade in modern times due to the extension of facilities of railway and steamer transport must not be regarded as a sign of industrial pre-eminence but rather as a necessary preliminary to it. If India develops her own manufactures, this will result, at least in the beginning, to a considerable diminution of her foreign trade, as she will be producing herself the manufactures which she at present imports from abroad. It may, however, happen that in the future her manufactures will develop to such an extent that after replacing foreign manufactures in the home market they will overflow her boundaries and spread in the outside world. In fact India's case may be cited in illustration of the uncertain connection between foreign trade and economic prosperity. While her first step forward in economic progress has been accompanied by a considerable *extension*, her next step will probably be marked by a *decline* of her international commerce, and the final stage in her economic evolution may again be characterised by an *increase* in her foreign trade.

INTERNAL TRADE.

§ 23. (A) Coasting Trade :—We have already indicated the present position and the future importance to India of her coastal trade in our discussion of the proposal to reserve the coastal trade for Indian shipping. The coastal trade may be regarded as a part of the inland trade of the country, though it also includes a small amount of foreign trade.*

The following table shows the value of private merchandise (Indian and foreign) imported and exported from the several maritime provinces of British India from and to Indian ports.

* In 1925-26, out of the total value of imports, viz., Rs. 111.88 crores, Indian merchandise was valued at 103.11 crores and foreign at Rs. 8.7 and similarly, out of a total value of exports of Rs. 99.46 crores, Indian merchandise was valued at Rs. 87.87 crores and foreign at Rs. 11.59 crores.

(In lakhs of Rupees)

	1916-17		1925-26	
	Imports	Exports	Imports	Exports
Bengal	12,92	7,07	20,68	16,82
Bihar and Orissa	14	10	13	27
Bombay	23,50	16,44	39,90	33,67
Sind	6,19	420	11,52	651
Madras	6,12	558	21,05	11,33
Burma	11,38	19,85	18,58	30,84
Total	60,28	53,27	1,11,88	99,46

Including the value of the exports and imports of government stores and of treasure, the total coastal trade was valued at 1,26,97 lakhs of Rupees and 2,18,05 lakhs in 1916-17 and 1925-26 respectively. The coasting trade between Burma and other provinces of India is of special interest as land communication with Burma is very difficult. The principal coastwise imports into Burma are coal, cotton piecegoods, jute bags, pulse, betel-nut, while the principal exports from Burma are rice, kerosine oil, petroleum, candles, lac, teak wood, timber, etc.\$

The total (imports and exports) foreign coastwise trade of the 8 principal ports of India in 1925-26 was as follows:—

(In lakhs of Rupees.)

	Foreign	Coastal	Total
Bombay	1,81,25	65,36	2,46,61
Calcutta	2,25,11	30,02	2,55,13
Rangoon	62,95	40,08	1,03,03
Karachi	62,39	17,91	80,30
Madras	32,58	9,07	41,65
Cochin	4,10	6,38	10,48
Tuticorin	8,53	5,05	13,58
Chittagong	8,32	6,00	14,32

\$ For further details see Review of Trade, 1926-27, p. 128.

These figures* show that Bombay, Calcutta and Rangoon to a very large extent, and Karachi and Madras to a smaller extent, account for the bulk of the total foreign and coastal trade of India.

For ensuring the fullest possible development of the coastal trade in India a comprehensive programme of port development, the building up of an Indian Mercantile Marine and a proper coordination between coastal and railway traffic are necessary, but these are topics on which we have already expatiated at considerable length.

24 (B) Inland Trade† :—India, like America, but unlike the United Kingdom, is more vitally interested in her internal than in her external trade. This is not surprising in view of the continental dimensions of the country, her teeming population, her diversity of physical and climatic conditions and her vast and varied natural resources. In modern times the extension of improved means of communication and transport have added greatly to the volume of the internal trade, and this process will be quickened by a general economic advance and the progress of organisation, which will increase the scope for exchange between town and country.

The great importance of the internal trade of India is insufficiently appreciated. The imposing figures of the exports of cotton, jute, rice, wheat, oil seeds, etc. represent only a moderate proportion of India's total production, of which some idea has already been given. Of course it is true that, not all that remains after export is offered for sale, for, a part of it is directly consumed by the producers, as in the case of the peasant proprietors, who consume a large portion of the food-stuffs raised by them. The great importance to India of her internal trade is brought out by the consideration that, "If India's total agricultural produce is taken into account, calculations show that for every acre of land producing goods, whether grain, oilseeds, fibres, tea etc. for export, eleven acres are cultivated for local consumption."¶ To

* Statistical Abstract 1925-26, pp. 442-444.

† See Vol. I. P. 218.

¶ See Worswick: op. cit. p. 145.

the agricultural production which remains in the country for internal consumption and exchange must be added the non-agricultural produce such as mineral production and manufactures, of which only a small percentage is exported abroad.

No accurate and reliable statistics are available regarding the volume and the value of the Inland Trade of the country. Fairly satisfactory data are available regarding the coastal trade, the bulk of which, as said above, may be regarded as a part of the internal or the inter-provincial trade of the country. But so far as the inland trade proper goes, scarcely any information beyond the statistics of the goods traffic of railways is available today. Until recently, the Department of Statistics used to publish annually the "Inland Trade (Rail and River-borne) of India," and all the provinces used to issue similar publications. These gave the import and export trade in staple articles of each of the five or six blocks into which every province was divided; and the imports and exports of eighteen bigger blocks forming the trade divisions of India as a whole. The figures related to the quantity only; the figures of value, given in a few cases were admittedly very rough. The internal trade returns were defective in other respects also. Trade within a block was not recorded, there was obvious evasion on railways, and trade by road, which is not negligible, was not taken into account. "† However, in spite of their defects these statistics were of some utility, and it is unfortunate that, except in one or two provinces they have been discontinued on the recommendation of the Retrenchment Committee. The Economic Enquiry Committee have rightly pressed for the revival of the publications of the internal trade returns and their improvement so as to bring them into line with the more up-to-date statistics of the same kind maintained by countries like the United States. In the absence of these publications the statistics published in the second volume of the annual report on Indian Railways, relating to the quantity of the principal commodities carried, is of some use, as giving an idea of the extent to which the different

† Economic Enquiry Committee's Report, p. 13.

parts of the country are concerned in the movements of the chief articles of trade. The following table shows the tonnage and earnings from the main commodities on Class I Railways (which account for 90 per cent of the total railways and for 97 per cent of the total traffic) in the year 1926-27.

Commodity	No. of tons originating in millions	Rs. in crores.
Fuel for public and Foreign Railways	18.95	9.65
Fuel and other stores on revenue account	16.13	2.89
Wheat	1.76	2.53
Rice in the husk and rice not in the husk	4.11	3.85
Gram and Pulse, Jawar and Bajra and other grains	3.05	4.35
Marble and Stone	2.99	0.88
Metallic Ores	2.45	1.04
Salt	1.42	1.89
Wood unwrought	1.32	0.89
Sugar refined and unrefined	0.77	1.88
Oilseeds	2.35	3.43
Cotton raw and manufactured	1.53	5.80
Jute raw	1.20	1.78
Fodder	0.80	0.60
Fruits and Vegetable fresh	1.08	0.91
Iron and Steel wrought	1.02	1.97
Kerosine Oil	0.92	2.04
Gur, Jagree, Molasses, etc.	0.78	1.19
Tobacco	0.26	0.66
Provisions	0.63	1.31
Military Stores	0.38	0.37
Railway materials	8.30	1.20
Live Stock	0.22	0.69
Other Commodities	9.65	11.44
Total	82.07	63.24

In the absence of full and dependable statistics relating to inland trade, no precise idea can be formed of its dimensions and of its relative importance as compared to the foreign trade of the country. According to the "Inland Trade of India for 1920-21," the total inland trade was estimated at nearly

Rs. 1500 crores thus giving a proportion of $2\frac{1}{2} : 1$ between the domestic trade and the foreign trade.* Such figures as are available, however, leave no doubt regarding the small volume of the inland trade in relation to the size and the population of the country. With a fuller development of the economic resources of the country the volume of internal trade is bound to increase to many times its present size.

§ 25. Principal Trade Centres of India¶ :—We may now fittingly conclude this chapter with a brief description of the principal trade centres of India followed by a few words about commercial intelligence and trade organisations. In an account of the trade centres of India mention may first be made of the five principal harbours of India, viz., Calcutta, Bombay, Karachi, Rangoon and Madras. Calcutta and Bombay are not only the principal ports but also the most important industrial centres of India. Bombay is further the chief distributing centre for Western India for the large volume of imports of cotton manufactures. The trade of Bombay is preponderantly in Indian hands as contrasted with Calcutta, where it is largely under the control of Europeans. Karachi is the centre of the wheat trade and Rangoon of the trade in rice, timber and oil. Madras also is a considerable trade and industrial centre but not comparable in importance to Bombay or to Calcutta. Apart from these five principal ports, other big trade centres are Cawnpore, Delhi, Ahmedabad, Amritsar, Agra, Lahore, Benares, Lucknow, Nagpur, etc. Cawnpore which is an important railway junction in the United Provinces holds a central position being situated halfway between Bombay and Calcutta and is a convenient distributing centre for foreign and local goods. Delhi, now the capital of India is the junction for nine railway lines and an important clearing house for the Punjab and the western districts of the United Provinces, particularly in cotton, silk and woollen piecegoods. Ahmedabad is next to Bombay the most important

* Prof. Shah holds that this is an under estimate and places the value of the inland trade of India at Rs. 2,500 crores. (See Trade, Tariff and Transport, p. 122).

¶ See Cotton op. cit. pp. 86-89.

centre in the Bombay Presidency. Amritsar in the Punjab has not only a large entrepot trade in piecegoods but also does a large business in skins and hides it is also well known for its carpet industry. Agra has considerable manufacturing industries connected with carpets, *daris*, embroideries and stone work and is a collecting centre for the better qualities of hides. Lahore is the chief trading centre for the agricultural produce of the Punjab. Benares is mainly of interest as a considerable centre of the silk weaving industry. Lucknow is commercially of interest as a distributing and collecting centre for the rich agricultural produce of Oudh. Nagpur derives its commercial importance from its weaving mills, cotton ginning and pressing factories and the extensive manganese deposits in its neighbourhood. In addition to these centres of trade, mention may also be made of Jubbulpore, Mirzapore, Madura, Gwalior, Dacca, Mandalay, Srinagar, Sholapur, Amraoti, Hyderabad (Deccan), Allahabad, Jaipur, Baroda, Bangalore, Mysore, etc.

§ 26. Commercial Intelligence and Trade Organisation:—The collection, careful analysis and judicious distribution of commercial and industrial intelligence has now come to be a necessary function of Government in civilised countries in view of the international competition in industry and commerce. Not a little of the prosperity of countries like Germany, Japan and the United States, etc. is owing to their excellent system of commercial intelligence. Trade commissioners are appointed and consuls stationed in foreign countries, their main duty being to supply information about foreign markets to their respective countries. India is insufficiently equipped in all these respects. Though the Commercial Intelligence Department came into existence as far back as 1905, it was put in evidence before the Industrial Commission that there was no clearly defined channel through which information on commercial matters in the possession of Government could be communicated, whether publicly or to individual applicants.* The Commission made several useful recommendations in this connection including the establishment of Indian trade agencies in other countries such

* Industrial Commission's Report, para 180.

as East Africa, Mesopotamia, etc. The position today is somewhat more satisfactory than it was a few years ago. The Department of Commercial Intelligence and Statistics, which was reorganised in 1922, now forms a connecting link between the commercial public and the Government of India. It collects information bearing on overseas trade which may be of use to Indian firms; compiles and publishes statistics of all-India importance relating to trade and so on. It answers trade inquiries, effects trade introductions and publishes in the Indian Trade Journal (the Weekly Organ of the Department) statistics and other information of commercial value. The Department keeps in touch with trade developments of interest to India. In the United Kingdom, through the medium of the Indian Trade Commissioner in London, who since 1926 has been assisted by the Trade Publicity Officer, opportunities as they present themselves in England for commercial publicity are utilised in India's interest. This step has led to some useful results. Since the appointment was made arrangements have been made for the display of Indian goods at some of the important exhibitions and fairs on the Continent.* The Department of Commercial Intelligence also works in cooperation with the British Trade Commissioners in India and the Dominions and with Consular Officers in the various parts of the world so as to stimulate the overseas demand for Indian produce and manufactures. The High Commissioner for India in London, whose office was created in 1920, has been saddled with much miscellaneous agency and financial work of which the purchase of Government Stores is the most important. He is therefore not in a position to be of much use for promoting Indian commercial interests abroad. The organisation described above is chiefly concerned with the publicity abroad of information regarding the possibilities of Indian markets for foreign goods. It is equally necessary, however, to supplement it by a similar organisation for the purpose of making available in India information regarding foreign markets for Indian goods. We have already stated that new ground has been broken in this direction and, on the recommendation of the Textile Tariff Board, a Trade Mission has been deputed to explore the potentialities of certain

* See *India in 1926-1927* p. 209.

export markets for the Indian textile goods. The establishment of Indian trade agencies and of an independent Indian consular service, as in the case of the self-governing Dominions, would be well justified as helping to develop trade relations with foreign countries on lines most beneficial to India.

§ 27. Commercial Organisation in India:—The most important and the best organised non-official commercial organisations in India are those formed by European merchants such as the Associated Chambers of Commerce, and the various Chambers of Commerce at Calcutta, Bombay, Madras, Rangoon, Karachi and other principal centres. Their membership, except in Bombay, is preponderatingly European, though open to Indians also. This is but the natural outcome of the earlier start made by European traders in establishing commercial connections between India and the West. In addition to the Chambers of Commerce there are also Associations representing particular branches of trade such as jute mills, cotton mills, etc.; and also those representing retail traders in the principal cities. Hitherto the Indian commercial community have suffered for lack of suitable organisation for obtaining redress for their legitimate grievances, and it is a welcome sign of the times that Indian merchants are waking up to the necessity of organising themselves. There are now several purely Indian associations such as the Indian Merchants' Chamber and Bureau, Bombay; The South Indian Chamber of Commerce, Madras; The Marwari Chamber of Commerce, Calcutta; and the more recently started Maharashtra Chamber of Commerce. All these organisations can be of immense service in focussing commercial opinion in India and giving a lead to Government in regard to problems affecting the commercial and industrial development of the country.*

* It may be noted here that some of the important Chambers of Commerce have been given representation both on the central and provincial legislative bodies.

CHAPTER VIII

CURRENCY AND EXCHANGE

§ 1. Indian Currency in the pre-British era:—Since Akbar's time the currency in Northern India had come to consist of the gold Mohur and the silver rupee, which both weighed 175 grains troy. There was no fixed legal ratio between them, though each of the coins bore a fixed ratio to the *Dam*, the copper coin of the Moghul Empire.* In Southern India which never came completely under the dominion of the Moghuls gold was the principal currency. Under Hindu rule, preference was generally given to gold, while the Mahommedans showed a predilection in favour of silver. When the Moghul Empire broke up and on its ruins arose a large number of independent states, many of them signalled their independence by striking a special coin, this being regarded as an insignia of sovereignty. Though the old denominations were generally retained, there was every degree of variation as regards weight and fineness. So that when the East India Company came upon the scene, it found that the currency position was characterised by a bewildering multiplicity and variety of coins of gold and silver. It has been calculated that as many as 994 different coins made of gold or silver and of varying weight and fineness were current.† The services of professional Shroffs (appraisers.) had constantly to be requisitioned for ascertaining the value of the coins held by the people. The East India Company found its commercial transactions seriously hampered by such a chaotic condition of the currency and thus began the series of experiments in currency organisation in India, whose history it is our purpose to narrate in this chapter.

§ 2. Four periods in the nineteenth century:—We may divide

* Ambedkar, *The Problem of the Rupee*, p. 3.

† Macleod, *Indian Currency*, p. 13.

the history of Indian Currency in the nineteenth century into four periods† :—

(1) The first period (1801-1835) is characterised by attempts to establish a uniform rupee as the only standard for the Company's possessions.

(2) The second period (1835-1874) is marked by efforts made to introduce a gold currency, and several proposals in this connection were discussed without, however, leading to the establishment of a gold standard and a gold currency.

(3) The third period (1874-1893) witnessed a continuous fall in the value of silver making the exchange value of the rupee low and unstable. During this period there was considerable agitation for currency reform on the basis of international bimetallism.

(4) The fourth period (1893-1900) is characterised by the closing of the Indian Mints to the free coinage of silver and the subsequent linking of the Indian currency with the gold standard a process completed in 1898 with the recognition of the British sovereign as unlimited legal tender side by side with the rupee with the fixed legal ratio of 15 : 1 between them.

We shall now deal with these four periods in more detail.

§ 3 The first period (1801 to 1835) :—The first attempt of the East India Company at evolving order out of the prevailing confusion in currency resulted in a simultaneous issue of both gold and silver coins with the Company's stamp, and with a definite legal ratio, weight and fineness. But owing to the fluctuations in the market value of the two metals it was found impossible to maintain the ratio. Under the official ratio gold was undervalued and was therefore displaced by silver. About this time Lord Liverpool published in England his famous Treatise on the Coins of the Realm, which enunciated the principle that only one metal should be the standard and unlimited legal tender, though other metals might also be coined and allowed to circulate at their market value. The Directors of the East India Company seeking for a way out of the currency

† See Findlay Shirras : *Indian Finance and Banking* p. 93. et seq.

muddle in India and influenced by Lord Liverpool's work selected silver to function as the only standard in India. However, in 1806, in a Despatch to the Governments of Bengal and Madras, they took care to mention that their intention was by no means to drive gold out of circulation where it was the general measure of value. The Company tried to keep the ratio between the rupee and the gold Mohurs, fixed but the latter were undervalued and disappeared from circulation. The recommendations of the Directors in 1806 had allowed discretion to the Indian authorities as regards the time and manner of giving effect to them, and they were not acted upon immediately. In 1818, however, the silver rupee of 180 grains $\frac{1}{12}$ th fine was substituted for the gold pagoda in the Madras Presidency. The coinage of gold pagodas in Madras was stopped, but for the convenience of the public it was announced that gold coins would be issued, and would be paid and received by all the public offices at such rates as may be determined by proclamation from time to time, the first rate chosen being 15:1.

In the meanwhile, the Bombay rupee had been made identical with the Madras rupee in 1823, and the last step was taken in 1835, when the Indian rupee in its present form and size was issued, being the same in regard to weight and fineness as the Madras rupee of 1818, and was made sole legal tender of payment throughout the territories of the East India Company. Mints were opened to its free coinage, and the Indian system came to be one of silver monometallism instead of the bimetallic or parallel standard system which had prevailed so far. The value of the silver bullion in the rupee and its legal value were identical. This Act remained in force up to 1893.

§ 4. Second period (1835-1874).—The Act of 1835, however, authorised the coinage of gold Mohurs and of five, ten, and thirty-rupee gold pieces at market value, if required by the public. In 1841, a proclamation was issued authorising the public treasuries freely to receive the gold Mohurs at their face value, that is to say, at the rate of 15:1 in payment of public dues. In 1848 and 1849, owing to the Australian and Californian gold discoveries, the price of gold fell in terms of silver.

Gold was overvalued in the official ratio of 15:1, and the holders of gold coins availed themselves of the opportunity of obtaining a larger price in silver than they could obtain in the market. People began to pay their public dues in the depreciated gold coins rather than in rupees, much to the embarrassment of Government. Lord Dalhousie's Government, therefore, withdrew the proclamation of 1841, and gold was thus definitely demonetised. These steps led to a great stringency in the money market which was particularly felt owing to the expansion of trade. After 1850 the production of silver was less than there was a demand for it. Also a large portion of silver rupees were being abstracted from circulation and being put to non-monetary uses. "The Mint was pitted against the smelting pot, and the coin produced by so much patience and skill by the one was rapidly reduced into bangles by the other."* There were no credit media to speak of to relieve the monetary stringency and banking was yet in an undeveloped condition. Under these circumstances people began to have recourse to their own remedy, as was pointed out by the Bombay Chamber of Commerce in a memorial to the Government of India praying for a gold currency, in which it was said that "there is an increasing tendency to the creation of a gold ingot currency, by the natives of this country, as a rude remedy for the defects of the existing silver one," and "that gold bars, stamped with the mark of Bombay Banks, are for this purpose circulated in several parts of the country."† The American cotton famine brought fancy prices in gold to Indian cotton exporters and gold was imported on a very large scale. There arose, therefore, a demand supported influentially by the three Chambers of Commerce for the introduction of a gold currency—a demand which was all the stronger, because the fear that had been felt about the depreciation of gold was largely belied by actual experience. In November 1864, therefore, the Government of India issued a notification by which sovereigns and half-sovereigns were to be accepted at Government Treasuries at the rate of rupees 10 and rupees 5 respectively and the Government of India were to pay the same to its creditors

* Cassels quoted by Ambedkar in *The Problem of the Rupee*, p. 34.

† Ambedkar ; op. cit, p. 42.

when convenient and if the latter desired to receive them in payment of claims against the Government. In 1866, the Calcutta Chamber of Commerce again urged the adoption of a gold currency, and the Government of India appointed the Mansfield Commission, which was the first of the committees and commissions, which have sat from time to time to deliberate upon the problem of the Indian currency and ladled out conflicting panaceas to cure the currency ills of the country. The Mansfield Commission recommended that (i) gold coins of 15, 10, and 5 rupees should be issued, as they were likely to be preferred by the people to notes of like values, and as the introduction of the gold currency would pave the way for the establishment of currency notes; and that (ii) the currency should consist of gold, silver and paper. But, for reasons which have never been clearly explained, no definite action was taken on the Report of the Mansfield Commission. In 1868, a Notification was issued by which the rate for the receipt of sovereigns and half-sovereigns was raised from Rs. 10 and Rs. 5 to Rs. 10-4 and Rs. 5-2 respectively, as the former rate was out of harmony with the market rate and failed to attract gold to the public treasuries. In taking these steps, without any explicit reference to the Mansfield Commission, Government showed their desire ultimately to make gold legal tender, but they wished to make sure of the fact as to the relative value of gold and silver in India before stereotyping the results by law and finally committing themselves to the legal tender of gold. In 1872, Sir Richard Temple submitted a note to the Government of India suggesting that a gold standard and currency was what was really wanted in India, and that a Commission should be appointed to decide definitely what should be the rating of gold and silver. The Council of the Governor-General was, however, not unanimous, and the second period in the currency history of India came to an end with the decision of the Government of India in 1874 not to accept the proposal.

§ 5. The third period (1871-1893).—From 1874 a great change had begun in the monetary status of silver. Germany demonetised silver in 1873. Sweden, Denmark and Norway followed in 1874, clos-

ing their mints to the free coinage of silver. The countries of the Latin Union had to fall into line, with the result that huge quantities of silver were thrown on the market. There was also an enormous increase of output of silver from new mines owing to improved processes. The demand for gold, on the other hand, was increasing owing to its introduction as the only standard in Europe and the United States and to the general expansion of trade, while the supply was declining. Gold and silver became in their relation to each other simply commodities with no connecting monetary link between the two. The depreciated metal began to flow on a huge scale into silver standard countries, and India more than ever became a sink for silver, which, as it came in, was largely coined into rupees by the Indian Mints. This heavy coinage was one of the causes which set up a decided tendency towards a rise of prices in India, though the phenomenon became much more marked after 1900, as we shall see later on. The fall in the price of silver is brought out by the following table.—

Year	Price of silver per ounce
1875	58 d.
1879	52½ d.
1888	43 d.
1892	37½ d.
1899	27 d.

With the depreciation of silver the exchange value of the rupee in terms of the sovereign, that is to say, its gold value began to move down and fell from about 2s. in 1871, to about 1 s. 2 d. in 1892. This is, however, anticipating matters to some extent. By way of picking up the thread of the narrative we have to notice that from 1874 up to 1878, the agitation for reform in India was directed chiefly to the closing down of the Mints for the free coinage of silver with a view ultimately to the adoption of the gold standard. In 1876, the Bengal Chamber of Commerce and the Calcutta Trade Association sent a memorial to the Governor-General requesting the temporary suspension of

compulsory coinage of silver by the Indian Mints. Government, however, refused to grant this request, being of the opinion that, without the substitution of gold as a standard, no such step was possible, and that they were not prepared to adopt the gold standard under the prevailing circumstances, which were still unsettled; and lastly, that the uncertainty in the situation was caused not only by the depreciation of silver but also by the appreciation of gold. In 1878, however, the Government of India themselves proposed to the Secretary of State that definite steps should be taken in the direction of a gold standard with a gold currency and that, in the meanwhile, the cost of the rupee should be increased to the public in India by charging an additional seigniorage in order to establish a definite relation between the gold coins and the rupee, which might, if necessary, be altered from time to time. The Secretary of State referred this proposal to the British Treasury which opposed the scheme on various grounds, and advised, with a somewhat pontifical air "that, it was better to sit still, than to have recourse, under the influence of panic, to crude legislation the result of which cannot be foretold and the effect of which cannot be measured." As an alternative to a gold standard, the Government of India pathetically clung for a long time to international bimetallism, with a devotion worthy of a Mrs. Micawber, when practically every other nation was deserting it. Between 1867 and 1899, there were no less than four International Monetary Conferences held to propose remedies for the currency difficulties in the different European countries and the United States. India was throughout inclined in favour of international bimetallism mainly because of her faith in its special use for herself as a means of rehabilitating silver in the currencies of the world, which, she hoped, would raise the price of silver and thus extricate her from her exchange difficulties. But the scheme fell through chiefly because of the opposition of England and the general desire on the part of the other European nations to adopt the gold standard in imitation of England, which led them to take up an attitude of hostility to the introduction of bimetallism in the silver-using countries. They feared that the demand which this would cause for gold on the part of the silver-using countries

would raise the price of gold to inconvenient heights and embarrass the countries of Europe, which were intent upon the establishment of their currencies on a stable gold monometallic basis.

§ 6. The fourth period (1893-1900);—In the meanwhile, the continued fall in the value of silver and the decision of the United States to repeal the Sherman Act, under which that government was required to purchase 54 million ounces of silver for annual coinage, made the position of silver and therefore the position of the Indian rupee more precarious than ever. Under these circumstances, the Government of India again approached the Secretary of State in 1891 with the proposal for closing the Indian Mints to the free coinage of silver with the object of eventually introducing the gold standard, if the International Monetary Conference then sitting at Brussels failed to arrive at any conclusion in favour of international action. Accordingly, in 1892, the Herschell Committee was appointed to consider the currency and exchange situation with special reference to the above proposal of the Government of India. While as yet the Herschell Committee was sitting, the Brussels Conference ended in a fiasco. The Herschell Committee had to suggest a remedy for the following principal defects of the Indian currency system as it then existed :—(1) The financial difficulties of the Government of India caused by silver monometallism and the falling rates of exchange with the gold standard countries. (2) The evil effects of the fall in exchange on the people of India and its commerce. (3) The difficulties caused by the fall in exchange to European officials in India. We shall now take these defects in the order in which they have been named and set forth more in detail the considerations arising from each of them.

§ 7. (1) The financial difficulties of the Government of India :—The difficulties of Government came principally from the fact that they had to remit yearly a very large sum to England in discharge of their gold obligations, viz., the Home Charges. The gold value of the rupee determined the actual incidence of this charge in India and, as we have seen, this value had been constantly falling

ever since 1874 and there was every prospect of its further fall. The inconvenience to Government of this state of affairs was well described by Sir David Barbour, the Financial Member of the Governor-General's Council from 1888 to 1893, as follows:—"The immediate cause of our financial difficulties, and the cause which, by comparison and for the time being, dwarfs all others, is the fall in the gold value of silver, which has added to the Indian expenditure in two years more than four crores of rupees. If that fall could be stayed and the rate of exchange with England fixed permanently at even its present low figure, the difficulty of dealing with the present deficit would be comparatively light. The revenue continues to grow in a satisfactory manner; even under the influence of indifferent seasons and poor harvests it has made fair progress. If we could feel assured that there would be no further fall in exchange, I have little doubt that increased revenue, restriction and reduction of expenditure, with possibly some taxation as a temporary measure, would, in a very short time, re-establish equilibrium. A serious effort would no doubt be required in the first instance, but with a fixed rate of exchange we would have a definite task before us, and our measures could be regulated accordingly. But it unfortunately happens that, unless some settlement of the currency question is obtained, there is no prospect of even the most moderate degree of stability in the rate of exchange.Our financial position for the coming year is at the mercy of the exchange, and of those who have it in their power to affect in any way the price of silver. If we budget for the present deficit of Rs. 1,595,100 and exchange rises one penny, we shall have a surplus; if it falls a penny, we shall have a deficit of more than three crores; if we impose taxation to the extent of one and a half crores of rupees, a turn of the wheel may require us to impose further taxation of not less magnitude; another turn, and we may find that no taxation at all was required. It will be obvious, from what I have just said, that what we have got to consider in making our arrangements for next year, is not so much the question of increasing the public revenue, or restricting that portion of the public expenditure

which is under our control, but the chances of a settlement of the currency question. " *

§ 8. Effect of fall in exchange on the people of India:— The increased number of rupees which the Government were required to find for meeting its sterling obligations meant more taxation in terms of rupees. This of course did not necessarily involve a permanent increase of the burden of taxation, for, in course of time adjustment would have taken place by a rise in silver prices in India, so that a larger number of rupees would have meant the same quantity of produce, and it is the quantity of produce and not the number of tokens representing it, that is the proper measure of the burden. A certain time, however, must elapse before the adjustment is completed, and in the meanwhile the Indian ryot would have to pay more in terms of produce. The Herschell Committee proceed to point out that although the burden upon the people as a whole may not eventually be greater on account of the fall in exchange, there was likely to be a transfer of burdens from one class to another. Owing to the fall in exchange, the burden of those who paid a fixed land revenue under a permanent settlement had been lightened and also of all those whose land revenue had not been recently resettled. On the other hand, the increased salt tax pressed upon the people at large, and rendered more heavy the taxation of those who had suffered rather than benefited from the higher rupee prices due to the fall in the gold value of silver.

Those in favour of the continuance of the silver standard argued that, the fall in exchange acted as a stimulus to exports, and that, although in theory it was unfavourable to imports, in actual fact, India's import trade had not suffered. Because the gold prices of these imports had fallen and were declining more rapidly than the gold value of the rupee, so that India was certainly not receiving from Europe smaller quantities of the goods she imported, on the average per rupee as well as per sovereign, than she was in 1872-73. As Kemmerer points out, " the actual development of the merchandise import and export trade during

* Quoted by Herschell Committee's Report, para 5.

the 20 years prior to the Herschell Committee Report had hardly been such as to justify a strong condemnation of the silver standard. ”*

Now as regards the stimulus to exports, this is clearly a transient benefit, as the exchange could not be expected to keep on descending indefinitely. Moreover, as against the stimulus to exports we must put the discouragement to imports. It may be that, owing to the fall in gold prices of imports, India was receiving as much of these imports as before the fall in exchange set in. But if the Indian exchange had not been declining and at the same time the gold prices were falling, India would have received even larger quantities of produce than she actually did. Leaving out of account temporary gains or losses to exports and imports respectively, another important argument against letting things alone was that, about 74 per cent. of the total imports of India came from gold-using countries, while 26 per cent. only came from silver-using countries. Intimate financial and commercial relations had thus been established with gold standard countries, and a constant fall in the value of the rupee must of necessity seriously embarrass India's foreign trade and had the result of introducing an unhealthy element of speculation into it. Further, even if the falling rupee conferred a temporary benefit on the employer in India, this was at the expense of the wage-earner, because wages rise more slowly than prices. Thus considering the benefit to India as a whole, it could not be said, that a continuous fall in exchange was an advantage.

In view of the difficulties caused both to Government finance as well as to the commercial community, it would be difficult to find much fault with the anxiety of Government to give up the silver standard in favour of the gold standard. The alternative method of increasing taxation, especially taxation in the form in which it would not have been unpopular, viz., by means of import duties, and of severe retrenchment in public expenditure, was no doubt not absolutely impossible. But given the prospect of constant fluctuations in the value of the rupee, continuous resort to taxation and economy would have been extraordinarily

* Kemmerer : *Modern Currency Reforms*, pp. 27-28.

difficult and unsettling in its effect. We repeat, therefore, that Government's desire to end all this uncertainty by switching the currency on to gold was natural and even commendable.

§ 9. Fall of Exchange and Foreign Capital:—The influence of a heavy fall in exchange was tending greatly to check the investment of British capital in India and the development of the country, which largely depended upon such investment. For, "London is the lending market, and London thinks in gold." The uncertainty as regards the interest on the investment and the prospect of the diminution which the invested capital might suffer, if it were desired to re-transfer it to England, impeded the flow of British capital into India. Foreign firms were also finding a difficulty owing to the falling exchange in procuring the services of European servants, required for conducting their undertakings in India. The difficulty in connection with attracting foreign capital to the country also had a prejudicial reaction on the finances of local bodies in India.

§ 10. Position of European Officials:—The Indian Government were also faced with difficulties as regards their own officers who began to put forward claims for compensation for the loss which they sustained owing to the fall in exchange. They received their salaries in rupees and for remitting a given amount in terms of sterling to England for the support of their families and the education of their children, they had to spend a larger and larger portion of their income than before. This had led to serious discontent amongst them.

§ 11. Recommendations of the Herschell Committee:— Having convinced themselves that the existing monetary system was in urgent need of reform the Herschell Committee proceeded to suggest remedies. Bimetallism being now out of the question, demonetisation of silver and the establishment of a gold standard currency might seem to be the only other alternative. But instead of this a sort of limping standard was recommended, under which there was to be no free mintage either of gold or of silver and the rupee was to continue to be unlimited legal tender, gold being used only partially for currency purposes during the

period of transition at the end of which further steps were to be taken to introduce a full-fledged gold standard.

§ 12. Government's action on the Report:—The Government of India approved of the Report, and after receiving the necessary authority from the Secretary of State proceeded to take action on it. In 1893, an act was passed to amend the Coinage Act of 1870, and the Indian Paper Currency Act of 1882. It provided for the immediate closure of the Indian mints to the free coinage of silver, though the Indian Government were allowed to retain power to coin rupees on their own account. There were also three administrative Notifications issued at the same time. The first provided for giving rupees in exchange for gold coin and bullion presented at the Indian mints, at the rate of 16d. to the rupee. The second Notification authorised the receipt of gold sovereigns and half-sovereigns in payment of public dues at the same rate. By the third Notification provision was made for currency notes being issued from the Paper Currency Offices, in exchange for gold coin or bullion, at the same rate.

The objects aimed at by these different provisions were first, to force up the exchange value of the rupee, or rather to arrest its further fall; secondly, to encourage the import of foreign capital; and thirdly, to familiarise the people with the use of the gold sovereign; and lastly, to discourage the import of silver. The general idea was to take the first steps towards the eventual introduction of the gold standard, and to link India with gold-standard countries immediately. It was thought that a period of transition was necessary before the actual establishment of the gold standard could be thought of.

§ 13. Circumstances leading to the establishment of the Fowler committee (1898):—The currency position from 1893 onwards was avowedly transitional and provisional, and some definite action still remained to be taken. This was hastened by the representations of the commercial community, who were inconvenienced by the famishing of the money market owing to the closing of the mints and the temporary suspension of the

sale of Council Bills, resulting in very high rates of discount. In the meanwhile, the rupee had been gradually gaining in exchange value, and the time seemed to have arrived for placing India definitely on a gold basis, or at least, to take a few further steps forward in that direction. This led to the appointment of the Fowler Committee in 1898.

§ 14. The Government of India's proposal:—The Committee considered several proposals. The first was that of the Government of India, which contemplated a further contraction in the volume of rupees so as to raise the value of the coin to ls. 4d. By 1898 the Government of India had come to the conclusion that silver should be definitely demonetised, and that steps should be taken with a view to the ultimate introduction of a gold standard. * The experiment of closing the Mints for silver appeared to have been highly successful from their point of view, as the rupee had steadily mounted up in exchange value since then, as the following statement shows:—

Calendar Year	Intrinsic value of rupee as silver bullion	Average exchange value of rupee	
		S.	d.
1894	$11\frac{1}{3}$ d.	1	$1\frac{1}{2}$
1895	$11\frac{3}{8}$ d.	1	$1\frac{3}{8}$
1896	$11\frac{7}{8}$ d.	1	$2\frac{1}{2}$
1897	$10\frac{1}{2}$ d.	1	$3\frac{1}{4}$
1898	$10\frac{3}{8}$ d.	1	$3\frac{7}{8}$

The Government of India made the following proposal as a first step towards the establishment of a gold standard:—

* In 1897 the Governments of United States and France tried to interest England in an attempt to bring about an international agreement with the object of securing a rise in the price of silver. They held large stocks of the metal, and its deterioration, which had been materially helped by the closing of the Indian Mints, was a matter of serious concern to them. The British Government asked the Government of India whether they would be prepared to re-open their Mints to silver again, but the latter having now made up their mind in favour of a gold standard summarily rejected the proposal.

(1) Money should be borrowed in England and part of it should be remitted to India in the form of gold to serve as the nucleus of a gold reserve. (2) About two and a half crores of rupees should be withdrawn from circulation and melted down in order to raise the gold value of the rupee to 1 s. 4 d.* (3) The silver bullion obtained by melting down the rupees should be sold for gold which was to be added to the reserve. (4) Government should not part with any of the gold in their possession until the exchange value of the rupee had risen to 1 s. 4 d. Till then gold was not to be made legal tender in India, though this was to be the future goal of currency policy.

This proposal was founded on the belief that, the contraction of currency relatively to the demand for it due to the closure of the Indian mints had been the real cause of the rise in the exchange value of the rupee, and that, so long as this cause continued to operate, a further rise in the exchange value might be expected, until eventually the rate of 1 s. 4 d. was established. The Fowler Committee were unable to agree with the view that, "the rise in the exchange value of the rupee was entirely due to the contraction of currency" and held that "the forces which affect the gold value of the rupee are complicated and obscure in their operation." They were therefore not prepared to recommend the drastic action proposed by the Government of India, especially as they feared that such action would accentuate the stringency in the Indian

* This showed Government's implicit faith in the quantity theory of money. But Nogaro points out that the simple relation between the rise of the rupee and the limitation of its quantity did not, as a matter of fact exist. For, the rise in exchange did not come about in the expected manner of first, a fall in internal prices, and then diminished imports and increased exports leading to a favourable exchange. In fact, Indian prices remained steady for nearly five years after the closing of the mints, between 1893 and 1897, and there was actually a sharp rise of prices in 1898. It is also significant that exchange stability was achieved in 1900 just when Government started minting rupees on a large scale. The real cause that sent up the exchange value of the rupee was the snapping of the link between the rupee coin and the metal silver of which it was made, making it possible for the former to rise in value while the latter was depreciating. In taking the measures they took, Government thus builded better than they knew from the point of view of gaining their object. See Bertrand Nogaro *La Monnaie* pp. 48-54, and Kale Vol II, p. 415 n.

money market and would provoke the opposition of the commercial classes.

§ 15. Probyn and Lindsay:—Among the other proposals which were placed before the Committee, special mention must be made of two, as they contained the germ of the gold exchange standard system, which later came to be actually adopted. These two proposals were put forward by Lesley Probyn who had retired in 1888 as Accountant-General of Madras, and A.M. Lindsay, Deputy Secretary and Treasurer of the Bank of Bengal respectively. Both these plans assumed that silver was better suited to India's domestic currency needs than gold, and that all that was necessary to do was to devise a scheme by which gold should be available for international purposes.

(a) *The Probyn Plan*:—Probyn laid great emphasis upon the hoarding habits of the people in India and deprecated any attempt to put gold coins into circulation, offering unusual temptation to the people to hoard or use them as ornaments. "If gold coins were passed into the currency," he said, "it would at first almost be like pouring water into a sieve." He therefore proposed that a new Government note should be issued of the denomination of Rs. 10,000 in exchange for gold and be made payable at the option of the holder either in rupees or in gold. The Currency Department should be empowered to pay either in sovereigns or in gold bars of the value of not less than £ 67 when gold was demanded by the public. Notes of smaller denomination were to be issued in exchange for silver rupees or gold, but were to be convertible at first only in rupees. As trade demand increased, exchange would rise to the gold import point and gold would be presented, at first in exchange for the large gold notes, and later on, for the smaller notes. Thus a sufficient gold reserve would gradually accumulate and enable Government to undertake the redemption of the notes in gold or rupees or rupee notes, provided these notes were presented in parcels of 10,000 Rs. The Fowler Committee rejected this plan on the ground that there was no successful precedent either in India or in Europe in support of such a use of gold bullion. They also thought that the plan displayed an undue nervousness with regard to the hoarding habits of the people. They pointed out that gold

coins had been in circulation in India before 1835, and held that if hoarding did not present obstacles to a gold circulation in the past, there was no reason why it should be made a ground for a permanent refusal to allow India to possess gold coins. In any case, the people of India would continue to satisfy their desire for the precious metals whatever the system of currency.

(b) *The Lindsay Scheme*:—The scheme suggested by Lindsay was a much closer approximation to the plan which was in fact introduced later on. It suggested the raising in London of a long period loan of £10 millions to be kept there as the Gold Standard Reserve. The arrangement of 1893 was intended to prevent the rise of the rupee above 1s. 4d. by making it binding on Government to give rupees in exchange for gold or gold sovereigns. Lindsay's aim was to supplement this plan by making arrangement for giving sterling in exchange for rupees so as to prevent the fall of the rupee below 1s. 4d. It was therefore proposed that the Government of India should sell in India sterling drafts on London for not less than £1,000 at the rate of 1s. 3 $\frac{3}{4}$ d. per rupee, which were to be paid from the reserve in London.

In London, rupee drafts were to be sold to applicants for not less than 15,000 rupees at the rate of 1s. 4 $\frac{1}{8}$ d. per rupee, and these were to be met at Calcutta and Bombay. If an excess of rupees accumulated in India, as the result of selling sterling drafts and consequently the reserve in London was unduly depleted, the excess of rupees was to be sold as bullion and the proceeds credited to the reserve in London. If, however, the stock of rupees in India was inadequate, silver was to be purchased out of the gold reserve in London and sent to India to be coined into rupees. The essence of this plan, as of the plan of Probyn, was that the rupee was to be the circulating medium in India, and gold was not to be legal tender. The Fowler Committee turned down the scheme, as they thought that the arguments against the Probyn plan told even more strongly against the Lindsay plan of an exchange standard. They feared that the adoption of the scheme would check that flow of capital to India upon which her economic prosperity so largely depended, and they objected that, if the system was made permanent in India, it would base India's gold standard for all time, on a few millions of gold in

London with a liability to pay in terms of gold in London for rupees received in India to an indefinite extent.

§ 16. Back to silver:—Another proposal before the Committee, which had now, however, the least chance of being accepted was a return to silver monometallism. The question of closing the Mints for silver had formed the subject of heated debate for a long time before the step was actually taken and had evoked strong opposition from official and non-official quarters. For example, Mr. R. Hardy, Treasurer and Secretary, Bank of Bengal, argued as follows in a memorandum which he submitted in 1886:—"The foreign trade of India consists of exports of merchandise; the exports pay not only for India's gold obligations abroad, but for her imports of merchandise as well, and a balance always remains in her favour. This balance she takes in silver. If silver is cheap she gets more of the metal than she would get if it were not so cheap, and I hold that it is most to her advantage to get more than less silver. It moreover appears obvious that the pressure of the gold payments upon India as a whole depends not upon the price of silver but upon the gold prices realised for the merchandise exported to meet such gold payments. That the Government is in the position of receiving its revenue in silver, it may be asserted, does not affect that, the national aspect of the question, and in my view it is therefore clearly the duty of Government to meet any financial necessity arising from a fall in the exchange, either by increasing taxation or by reducing expenditure, or by both. To attempt to meet the difficulty by taking the extreme measure of changing the standard of value is, I think, out of the question, and I express this view, holding the opinion that the value of silver will probably yet fall considerably."

Similarly, Mr. J. Westland, Controller and Auditor-General wrote in 1886:—"I am inclined rather to say that greater facility in meeting its home obligations is the *only* interest that India has in a gold standard; and if a silver standard is better with respect to all its other relations and concerns, I cannot concede that the question connected with its home obligations is of such tremendous importance as to overwhelm all others. The fact that our European officials, regarding our connection

with India as only temporary, look to the gold standard of the country, where we ultimately intend to live, as preferable for our own purposes, to the silver standard of the country where we earn our living, is somewhat apt to increase in our eyes the importance of remittance from India to England. But if we wanted to stay in India all our lives, and our children after us, as the definite majority of people dwelling in India do, I doubt if we would look upon a manifestly appreciating standard as more desirable than one which has been fairly steady in the past, so far as absolute value can be measured."

Mr. David Barbour, when he was Secretary to the Government of India in the Department of Finance and Commerce, was amongst the strongest opponents of a gold standard for India, and held that, "the loss or gain to India as distinguished from the Government of India, in respect of her permanent gold obligations depends entirely on the gold prices which she can obtain from her exports. No manipulation of the Indian currency can possibly affect the gold prices of Indian exports and give any relief to India as a country, whatever effect it might have on the financial position of Government. Just as much as Government gained, just so much must the Indian people lose."*

By 1893 however, the opposition to the closing of the Mints to silver had abated considerably, and it is significant that Barbour, who had some years ago vigorously opposed the plan, was himself the Finance Member, and as such sponsored the change of 1893. He had been of opinion that the salvation of India lay in international bimetallism. When, however, he found that that idea was impossible of accomplishment he transferred his allegiance to the gold standard. And when five years later it fell to the Fowler Committee formally to consider the question of re-opening the Mints, it found that there were comparatively few advocates of the silver standard left. Even Sir James Westland, whose opinion against the abandonment of the silver standard has been quoted above, opposed its restoration in 1898 in his capacity of Finance Member to the Government of India. He now regarded the demonetisation of silver

* All these three extracts are quoted by Kale:op. cit. Vol. II pp. 420-422.

as an accomplished fact and stuck to an honest interpretation of the gold standard as implying the closure of the Mints for the coinage of silver not only for the public but also for Government itself. This is what he said in 1898, when a demand was made by some people that Government should resume the coinage of rupees for relieving monetary stringency: "In our opinion, the silver standard is now a question of the past. It is a case of *vestigia nulla retrorsum*. The only question before us is how best to attain the gold standard. We cannot go back to the position of the open Mints. There are only two ways in which we can go back to that position. We can either open the Mints to the public generally or we can open them to coinage by ourselves. In either case, what it means is that the value of the rupee will go down to something approaching the value of silver. If the case is that of opening the Mints to the public the descent of the rupee will be rapid. If it is that of opening only to coinage by the Government, the descent of the rupee may be slow but it will be no less inevitable."

§ 17. Recommendations of the Fowler Committee:—The Fowler Committee had thus not much difficulty in rejecting the plea for the restoration of the silver standard, as no fresh arguments had been brought forward, and the actual discontinuance of the silver standard since 1893 had sensibly weakened the case for it. It concluded, on considering the evidence placed before it, that the ideal to be aimed at was the "effective establishment in India of a gold standard and currency based on the principles of the free inflow and outflow of gold," and with this end in view made the following proposals:—(i) The Indian Mints should be thrown open to the coinage of gold sovereigns and half-sovereigns on terms and conditions such as governed the three Australian Branches of the Royal Mint. The Mints should remain closed to the free coinage of silver as already decided in 1893, "until the proportion of the gold in the currency is found to exceed the requirements of the public." (ii) The exchange rate was to be finally fixed at 1s. 4d. per rupee, as this was the rate that had already been established, and, prices having been adjusted to it, it would be easier to maintain than any other ratio. (iii) The rupee might continue to be unlimited legal tender, for,

so long as the principle of limitation was in effective operation, and no fresh rupees were coined, the value of the rupee would be maintained at the ratio decided upon, and it was not necessary to make it also limited legal tender for this purpose. (iv) Government should continue to give rupees in exchange for gold, though they should not bind themselves to give gold in exchange for rupees, because the undertaking of such an obligation would be inconvenient and make Government liable to sudden demands for gold, to meet which it may sometimes be necessary to raise sterling loans at a heavy cost. (v) For securing the convertibility of the rupees into sovereigns, the profits on any future silver coinage undertaken by Government should be credited to a gold fund to be kept "as a special reserve, entirely apart from the Paper Currency Reserve and the ordinary treasury balances." For, although no legal obligation of converting rupees into gold was to be imposed on Government, it would be an advantage if they could pay out gold whenever their reserves permitted and the people were willing to accept it. (vi) Government should be prepared to make gold available, particularly for export when the balance of trade goes against India. The Committee expected this gold to come from the gold reserves generally and especially from the gold fund proposed by it, but eventually also from circulation, when the latter should be saturated with a large amount of gold as the result of the full introduction of a gold standard and gold currency.

In short, the Fowler Committee held that a fixed exchange could only be secured and guaranteed by an effective gold standard. The Committee accepted as their model, the limping standard adopted by the Latin Union and the United States, under which both gold and silver were unlimited legal tender with a fixed legal ratio, and mints were open only to the free coinage of gold. The recommendations of the Fowler Committee were accepted almost entirely by the Government of India, and the Act of the year 1899 made sovereigns and half-sovereigns legal tender throughout India at the ratio recommended by the Fowler Committee.

Negotiations were also set on foot for starting a gold mint in India but proved abortive on account of the opposition of the British Treasury.

A Gold Standard Reserve was formed in 1900 out of the profits of the coinage of rupees on Government account which was resumed for the first time after 1893,

§ 18. Remedies adopted in relief of monetary stringency :—

(i) *Circulation of gold*—After the above action had been taken in faithful compliance with the Fowler Committee's recommendations, Government policy soon got loose from its moorings and drifted aimlessly until it landed into the patchwork of improvisations called the Gold Exchange Standard. The Fowler Committee had recommended that fresh coinage of rupee should not be undertaken until the proportion of the gold in the currency was found to exceed the requirements of the public. Government, however, were forced to resume coinage under the pressure of a number of circumstances. The closing of the Mints had resulted in a stringency which was felt keenly as trade expanded and population increased. As a temporary measure for meeting the situation, Act II of 1898 was passed by which "the proceeds of the Secretary of State's sales of Council Bills could be set aside at the Bank of England in gold as part of the Indian Paper Currency Reserve. The Government of India could issue notes against the gold so set aside, and with them could meet *pro tanto* the Secretary of State's Drafts, without reducing their treasury balances." * This had the effect of adding to the drain on the stock of rupees with the Government of India. In order both to familiarise the people with gold coin and to obviate the necessity of fresh coinage of rupees. Government made an active attempt in 1899 and 1900, to introduce sove-

* As Kemmerer points out, this measure was practically an adoption of the Lindsay Plan, by Government, a year before the Fowler Committee's Report recommended its rejection—a recommendation which was accepted by the Indian Government. For it meant "the sale of exchange in London by the Secretary of State on the Paper Currency Reserve in India, at rates representing practically the gold-export point for London, with the primary object of releasing currency to meet monetary demands in India." Kemmerer : op. cit. p. 102.

reigns into circulation by instructing Post Offices, Paper Currency Offices, District Treasuries and Railways to encourage receipts and payments in the form of gold coin. Many of the gold coins thus issued, however, were soon returned to Government, who regarded this as a failure of the experiment to induce people to use sovereigns as the medium of exchange. Government, however, seem to have admitted defeat too soon and too readily, and even among their own officials there were not wanting some who saw no reason to be dissatisfied with the actual results of the experiment. Sir C. E. Dawkins remarked in the course of his Financial Statement for 1900-01, "I believe that the rate at which gold is taken is likely to increase slowly, and that gold will pass gradually into general circulation in our seaports and large towns. No expectation was ever formed, nor is there any reason to desire, that gold would penetrate into the interior, or that the large mass of transactions in the country would ever be conducted except through the medium of silver and copper. Gold is behaving very much as we anticipated."* Dr. Cannan also regards the alleged dislike for gold on the part of the Indian people as a myth. The allegation, he says, "is suspiciously like the old allegation that the "Englishman prefers gold coins to paper, which had no other foundation than the fact that the law prohibited the issue of notes for less than £ 5 in England and Wales, while in Scotland, Ireland, and almost all other English-speaking countries notes for £ 1 or less were allowed and circulated freely. It seems much more likely that silver owes its position in India to the decision which the Company made before the system of standard gold and token silver was accidentally evolved in 1816 in England, and long before it was understood; and that the position has been maintained not because Indians dislike gold, but because Europeans like it so well that they cannot bear to part with any of it."†

The experiment was not only not persisted in sufficiently long but the circumstances under which it was launched were also exceptionally unpropitious, because the famine conditions which

* Quoted by Wadia and Joshi: *Money and the Money Market in India*, p. 204.

† Dr. Cannan's Foreword to Ambedkar's *The Problem of the Rupee*, p. xiii.

prevailed intensified the demand for *rupees*. Sir Edward Law, the Finance Member, explained the phenomenon thus: "The great bulk of the population is purely agricultural. The agriculturist, in ordinary times, has little requirements for money in the shape of silver coin; he is himself the producer of a large proportion of the food he consumes, and his other wants which must be satisfied by purchase are trifling. In seasons of famine, however, the situation is changed. The food consumed by the suffering agriculturists must be purchased and paid for with coin, and as credit dries up in times of distress all his other requirements must equally be paid for in cash." R.G. Hawtrey in his *Currency and Credit** criticising this view remarks that Sir Edward Law's explanation of the intensified demand for rupees in 1899-1900 "was no more than an ingenious conjecture." According to him the demand occurred at a period of good trade. He admits it as a most striking fact that the period of rising exchange from 1896 to 1900 was marked by *two* severe famines, one in 1896-97 and the other in 1899-1900, and this gave a certain plausibility to the theory put forward by Sir Edward Law. All the same he rejects the theory and argues that there may be more cash *transactions* in a time of famine than in a time of plenty, but that does not mean that people will hold larger cash *balances*.

(ii) *Issue of Notes and Rupees*:—However that may be, Government found themselves forced to resume coinage on a large scale in 1900. The silver required for this purpose was purchased with the gold in the Paper Currency Reserve in London. We have already referred above to Act II of 1898 by which the receipts from the sales of the Secretary of State's Council Bills were set apart in the Paper Currency Chest, and notes were issued in India against them. This was intended to be a purely temporary arrangement and the Act provided that the gold so set apart was to be held by the Secretary of State in London, "until he shall transmit the same in gold coin or gold bullion to India, or until the Government of India shall appropriate and set apart in India as a part of the Currency Reserve an amount of coin of the Government of India equal in value to such notes." This Act

* pp. 345-347.

was extended in the first instance for two and a half years, and again for two years more in 1900, when the Secretary of State was authorised to use the gold so received by him for the purchase of silver bullion to be sent to India for being coined into rupees, and to treat such bullion in transit and in process of coinage as part of the Paper Currency Reserve. The Reserve in London was thus made to serve three distinct purposes. (i) It provided funds in London for the purchase of silver for coinage whenever necessary. (ii) It could be used to support the Indian exchange, whenever India had an unfavourable balance of trade and it was impossible or disadvantageous to sell Council Bills. The Secretary of State would, under these circumstances, use the gold in the Paper Currency Reserve for meeting his expenses and an equivalent amount would be transferred to the Paper Currency Reserve in India. (iii) And lastly, it was a fund into which payments might be made by the Secretary of State whenever he sold Council Bills in excess of his requirements in order to prevent exchange from rising unduly high† and inducing an undesirable shipment of gold to India. Against these payments notes would be issued in India.

In 1902 these provisions were made permanent. In 1905, £ 5 millions, that had accumulated in the Reserve in India, were shipped to London to be held in the Paper Currency Chest of ear-marked gold (not to be used for ordinary expenses) at the Bank of England, and a stated part of the Currency Reserve was invested in sterling securities. Since 1906 a substantial part of the Paper Currency Reserve has been maintained in the form of gold.

§ 19. The Gold Standard Reserve:—In the year 1900, the Government of India proposed the constitution of a Gold Reserve to be kept in India as desired by the Fowler Committee. They proposed further that the Paper Currency Reserve should gradually revert to its original position and should be used only for the encashment of currency notes and further that they should consist principally of rupees and securities. The Gold Reserve, on the other hand, should consist chiefly of gold. The Secretary of State, however, decided against this. He preferred to have the gold located in London and invested in sterling securities. He

† See § 20 below.

held that, since London was the place in which the Reserve would have to be applied on the occasion of the emergency against which it was being created, London would be the best place in which to keep it. In this manner, instead of being used primarily as a gold redemption fund and for the maintenance of the exchange parity of the rupee, the Gold Reserve came to be regarded merely as part of the total surplus funds of Government and as a kind of 'secondary reserve.' The work of maintaining the parity of the rupee fell chiefly on the Paper Currency Reserve and the sale of Council Bills in London, "with the result that the three funds, viz. the Paper Currency Reserve, the Gold Reserve, and the Secretary of State's balances, soon found their functions confused, the properly fiscal function of the last fund and the properly monetary function of the other two being sadly mixed."

* According to the plan insisted upon by the Secretary of State, the profits from the coinage of rupee were remitted to London for investment and this was effected by gold being withdrawn from the Paper Currency Reserve in London in exchange for the fresh rupees coined in India. In 1906 the difficulty in meeting the demand for rupees led to the formation in India of a special Rupee Reserve outside the Paper Currency Reserve, called the Silver Branch of the Gold Standard Reserve.¶ The Rupee Reserve was intended to prevent the exchange from rising above 1s. 4d., which necessitated the keeping open of an unlimited offer of rupees in exchange for sovereigns at this rate in India. The Notification of 1893 which had authorised the issue of rupees or notes against the tender of gold as distinguished from the British gold coin was withdrawn. In the meanwhile, the practice of shipping to London gold accumulated in the various Reserves in India was found to be needlessly expensive, and, therefore, the practice of selling Council Drafts was extended beyond its original purpose since the year 1904, when the Secretary of State announced his intention

* The account that follows is based mainly on the Chamberlain Commission's Report.

¶ The Gold Reserve came to be known as the Gold Standard Reserve from this date.

of offering Council Bills for sale without limit of amount at the price of 1 s. $4\frac{1}{8}$ d. If the cash balances in India were inadequate for this purpose, the demand was to be met by withdrawing rupees from the Paper Currency Reserve in India, an equivalent amount of gold being credited to the Paper Currency Chest in London. The price of 1s. $4\frac{1}{8}$ d. not being found prohibitive at all times of the export of sovereigns to India, which accumulated with the Indian Government, it was decided to offer Telegraphic Transfers against sovereigns in transit from Egypt and Australia to India, the rate for the Transfers being between 1s. 4d. to 1s. $4\frac{1}{2}$ d. (i.e. lower than that for the Council Bills.)*, so as to make it worth the while of the owner of such sovereigns to divert them from India to London.

In June 1907, the Mackay Committee on Indian Railway Finance recommended that one million sovereigns out of the profits on the coinage of rupees in 1907 should be spent on Railways. The Secretary of State went beyond the Committee and decided to spend on Railways in the future, one-half of any profits on the coinage of rupees, until the Gold Standard Reserve reached £ 20 millions, apparently contemplating the diversion of the *whole* of the profits to the Railways after the maximum had been reached. The Government of India telegraphed to the Secretary of State that, the portion of the Gold Standard Reserve in the form of sterling securities should be allowed to accumulate up to £ 20 millions before any such diversion was effected. The Secretary of State disapproving adhered to his decision, which, however, he had to reverse completely in 1909, owing to the exchange crisis of 1907-08.

§ 20. The crisis of 1907-08 :--On account of a partial failure of crops in some parts and the outbreak of actual famine in others, Indian exports declined. In Europe also, after a period of prosperity, which reached its culmination in 1907, a decline set in leading to unemployment and slack business. The purchasing capacity of Europe was thus impaired and the situation was aggravated by the general monetary stringency caused by a financial crisis in New York. While Indian exports of jute, wheat,

† For a detailed explanation of the working of this system see Keynes *Indian Currency and Finances*, pp. 114 to 118.

cotton, etc., fell off, the imports rose, at least in the case of one commodity, viz. silver owing to a heavy fall in its price. All these factors contributed to the weakening of the Indian exchange. The stock of sovereigns began to diminish rapidly, and the Exchange Banks urged Government to sell Telegraphic Transfers on London. This was refused by Government, who, however, gave gold on certain conditions (not more than £10,000 to any one individual on any one day) from the Paper Currency Reserve. The situation growing worse, the Secretary of State advised the Government to offer Telegraphic Transfers or Reverse Councils on London at the rate of 1s. 3 $\frac{2}{3}$ d. per rupee, and himself released gold from the Paper Currency Reserve in London, against a transfer of rupees to it from the Treasuries in India. He had also to float a sterling loan of £4½ millions to keep up his finances, as no Council Bills could then be sold. He met the demand for the encashment of the Reverse Councils sold on him by selling the sterling securities in the Gold Standard Reserve in the market, even although they had depreciated in value. These measures brought about an improvement, and next year exchange was steady at 1s. 4d., the revival of the export trade from India coming to the rescue.

§ 21. Gold standard or Gold Exchange Standard?—In meeting the crisis Government had taken certain steps in a somewhat subconscious and tentative manner in the direction of the Gold Exchange Standard. Gold was at first given freely in exchange for rupees for internal use, whereas there was considerable reluctance displayed, to begin with, in providing gold for private export abroad. This showed that Government had not yet clearly thought out and definitely adopted the Gold Exchange Standard system. But the subsequent sale of Reverse Councils established a precedent, which brought the Indian currency system appreciably nearer the Lindsay Plan. The practice of paying out rupees and notes in India against deposits of gold in the Paper Currency Reserve in London had already been in vogue for some time, and in 1904, the Secretary of State had declared his willingness to keep the tap turned on indefinitely and sell the Council Bills to an unlimited amount at a fixed rate. In 1907–08 the sale of Reverse Councils providing for the conversion of

rupees into sterling for international purposes, may be said to have put the coping stone to the edifice of the Gold Exchange Standard.

All the same, however, the Government of India, had not yet formally accepted the whole gospel of the Gold Exchange Standard, and for some time after the crisis of 1907-08, we find them occupied in putting forward proposals which diverged as regards important particulars from the Gold Exchange Standard system as it came to be established eventually. For example, they had not yet reconciled themselves completely to the location of the Gold Reserve in London and had not quite made up their mind about preventing the circulation of gold as a currency medium in India.

The steps taken in order to meet the crisis had resulted in a serious depletion of Government's gold resources. In London, the sovereigns in the Currency Chest were reduced from £ 7 millions to £1½ millions, while in India the whole stock of gold was exhausted.* Government were thus impressed with the necessity of enlarging the Gold Reserve so as to enable them to meet such crises with greater equanimity in the future. In 1909, they proposed to the Secretary of State that £ 25 millions should be regarded as the minimum necessary for safety, and that, until this figure was reached, no portion of it should be diverted for capital expenditure on Railways. They also recommended that the Gold Standard Reserve should be maintained in a more liquid form.

The Secretary of State replied that £ 25 millions *both* in the Gold Standard Reserve and the Paper Currency Reserve together would, in his judgement, be the proper standard, and that so long as this combined total was not reached, no diversions would be made from the Gold Standard Reserve, and that the question might be reconsidered thereafter.

He did not wholly agree to the other proposal about maintaining the Reserve in a liquid form, but decided to keep £1 million of the Gold Standard Reserve liquid by allowing this amount to be

* See H. F. Howard: *India and the Gold Standard*, p 35.

lent for short periods on approved securities to approved borrowers in London and invest the rest in high-class securities with a near date of redemption, or in Consols and other approved stock.

In 1912, in deference to the wishes of the Government of India and in view of public criticism in India, the Secretary of State decided that £ 25 millions in gold should be ear-marked on behalf of the Reserve as a deposit in the Bank of England.

In taking the various steps described above Government had almost in spite of themselves steadily deviated from the strait and narrow path of the gold standard recommended by the Fowler Committee, and by a succession of opportunist measures were finally led into the scheme propounded by Lindsay. The system as it developed had not been thought of in 1893 and was opposed both by Government or by the Fowler Committee in 1899, nor is it possible to point to any single date at which it may be said to have been deliberately adopted.

Proposals for gold coinage and a gold mint were revived at the instance of Sir Vithaldas Thackersey, who moved a resolution to that effect in 1911 in the Imperial Legislative Council. Negotiations in this connection lasted for about a year, when it was decided to refer this question along with others to a Currency Commission which was contemplated.

§ 22. The Chamberlain Commission:—The Commission was necessitated by persistent and severe criticism of Government's currency and exchange policy. It was appointed in April 1913 with the Right Hon. Mr. Austen Chamberlain as its Chairman, and reported in February 1914. Its conclusions and recommendations were as follows:—*

(1) The establishment of the exchange value of the rupee on a stable basis is a matter of the first importance to India. (2) The measures adopted for the maintenance of the exchange value of the rupee have been necessarily and rightly rather supplementary to, than in all respects directly in pursuance of, the recommendations of the Committee of 1898. (3) The crisis of 1907-8 was the only occasion upon which they had been

* Chamberlain Commission's Report, para 223.

severely tested and they were found to work satisfactorily then. Owing to lack of experience in working the machinery and the absence of any plans fully worked out in advance for dealing with such a crisis, Government did at first make mistakes. For example, the India Office seemed to believe that the sole, or at least the main, purpose of the Gold Standard Reserve was to meet the requirements of the Secretary of State in London, when Council Bills could not be sold, while the Government of India made the mistake of refusing to give gold from the Paper Currency Reserve for export, though allowing their gold to be drained away for internal uses. Both the authorities failed to realise that the principal use of a gold reserve is that it should be freely available for foreign remittances whenever the exchange falls bellow specie point. These mistakes, however, were very quickly rectified in practice, and the steps taken to restore and maintain exchange proved adequate. (4) The history of the previous 15 years showed that a gold currency in active circulation was not an essential condition of the gold standard, which had been firmly secured without this condition. (5) It would not be to India's advantage to encourage an increased use of gold in the internal circulation. (6) The people of India neither desire nor need any considerable amount of gold for circulation as currency, and the currency most generally suitable for the internal needs of India consists of rupees and notes. (7) A mint for the coinage of gold is not needed for purposes of currency or exchange, but if Indian sentiment genuinely demands it and the Government of India were prepared to incur the expense, there was no objection in principle to its establishment either from the Indian or the Imperial standpoint provided that the coin minted was the sovereign (or the half-sovereign); and it is pre-eminently a question in which Indian sentiment should prevail. (8) If a mint for the coinage of gold is not established, refined gold should be received at the Bombay mint in exchange for currency. (9) The Government should aim at giving the people the form of currency which they demand, whether rupees, notes or gold, but the use of notes should be encouraged. (10) The essential point was that this internal currency should be supported for exchange purposes by

a thoroughly adequate reserve of gold and sterling. (11) No limit should be fixed to the amount up to which the Gold Standard Reserve was to be accumulated. Reliance ought to be placed on the Paper Currency Reserve for the support of exchange only in so far and so long as the Gold Standard Reserve was not adequate to support the burden by itself. (12) The profits on the coinage of rupees should, for some time at least, continue to be credited exclusively to the Reserve. (13) A much larger proportion of the Reserve should be held in actual gold. By an exchange of assets between this Reserve and the Paper Currency Reserve, a total of about £ 10 millions in gold could at once be secured. This total should be raised as opportunity offered to £15 millions, and thereafter the authorities should aim at keeping one-half of the total Reserve in actual gold. While it is unnecessary and wasteful to hold the whole of the Gold Reserve in gold, the loss from enforced realization of securities in a time of crisis should be guarded against by maintaining a sufficient amount in liquid form. (14) The Indian branch of the Gold Standard Reserve should be abolished as it had given rise to much criticism, and was responsible for much confusion and doubt as to the efficiency of the Reserve. (15) The proper place for the location of the whole of the Gold Standard Reserve is London. (16) Government should definitely undertake to sell bills in India on London at the rate of 1 s. $3\frac{2}{3}$ d. per rupee whenever called upon to do so.

The Commission thus gave their most unstinted approval to the non-descript currency system, which had been evolved fortuitously. Government had not always felt very comfortable under it, and responsible officials still spoke occasionally as if they regarded the Gold Exchange Standard, under which India found herself, as merely a way-side inn, the real destination being a gold standard with its usual accompaniment of a gold currency.*

* Sir James Meston speaking in the Budget debate used the following words:—

“ We have linked India with the gold countries of the world. We have reached a gold-exchange standard, which we are steadily developing and improving. The next and final step is a true gold currency. That, I have every hope, will come in time, but we cannot force it. The backwardness

In 1912, the Government of India, in sympathetic response to the agitation in the country in favour of a gold mint in Bombay which culminated in Sir Vithaldas resolution referred to above, addressed the Secretary of State on the subject urging him not to turn a deaf ear to the popular demand for a gold coinage. The Chamberlain Commission, however, attempted to give a new turn altogether to Government's thoughts. They practically assured them that, without knowing it, they had put India into the forefront of nations in currency matters by adopting the Gold Exchange Standard system.

§ 23 The Mechanism of the Gold Exchange Standard:—Mr. J. M. Keynes one of the ablest exponents of the system which was thus extolled and which remained in full operation from 1898-99 to 1915-16, summarises and explains its main features as follows:—* “(1) The rupee is unlimited legal tender and, so far as the law provides, inconvertible. (2.) The sovereign is unlimited legal tender at £ 1 to 15 rupees and is convertible at this rate, so long as a Notification issued in 1893 is not withdrawn, *i. e.*, the Government can be required to give 15 rupees in exchange for £ 1. (3) As a matter of administrative practice, the Government is, as a rule, willing to give sovereigns for rupees at this rate; but the practice is sometimes suspended and large quantities of gold cannot always be obtained in India by tendering rupees. (4) As a matter of administrative practice, the Government will sell in Calcutta, in return for rupees tendered there, bills payable in London at a rate not more unfavourable than $1s. 3\frac{2}{3}d.$ per rupee.†

of our banking arrangements, the habits and suspicions of the people, the infancy of co-operation—all stand in the way. But the final step will come when the country is ripe for it. I trust that it will not long be delayed; for when it comes, it will obliterate all the mistakes, all the inconveniences, all the artificialities, of our present position.” quoted by Keynes: *op. cit.*, p. 67.

* Keynes: *op. cit.* pp. 6-7.

† Elsewhere, Mr. Keynes describes the essentials of the Gold Exchange Standard as “the use of a local currency mainly not of gold, some degree of unwillingness to supply gold locally in exchange for the local currency, but a high degree of willingness to sell foreign exchange for payment in local currency at a certain maximum rate; and to use foreign credits in order to do this.” See *Indian Currency and Finance*, p. 29.

The fourth of these provisions is the vital one for supporting the sterling value of the rupee; and although the Government have given no binding undertaking to maintain it, a failure to do so might fairly be held to involve an utter breakdown of their system.

Thus the second provision prevents the sterling value of the rupee from rising above 1 s. 4 d. by more than the cost of remitting sovereigns to India, and the fourth provision prevents it from falling below 1 s. $3\frac{2}{3}$ d. This means in practice that the extreme limits of variation of the sterling value of the rupee are 1 s. $4\frac{1}{8}$ d. and 1 s. $3\frac{2}{3}$ d."

It is claimed for the Gold Exchange Standard that, while it is much cheaper than a gold standard and gold currency, it ensures all the advantages of the latter. In India, it is obvious that the principal object of the system has been the maintenance of the rupee at par with gold. When exchange shows signs of weakness, Government come out as sellers of sterling (Reverse Councils), and when the rupee is tending to appreciate, they come out as sellers of the local currency (Council Bills). And the effectiveness of Government interference in this manner depends upon the adequacy of their gold and rupee reserves.

§ 24. Government resources and the claims on them:—The Chamberlain Commission have well described the nature of the resources available to the Government and the principles governing their use as follows:—"The first principle to be borne in mind in any consideration of the Indian finance and currency system is that the balances of the Government of India in India, and of the India Office in London, and the portions of the Gold Standard and Paper Currency Reserves located respectively in India and in London, all represent in the last analysis one single fund. The titles attached to the constituent portions of this fund indicate to some extent the nature of the needs and liability for which the fund as a whole is required to provide. The name attached to each portion indicates the primary function of that portion; but neither in theory nor in practice have the separate portions of

* See Report, pars 9-10

the fund been entirely reserved for the objects indicated by their separate names.

The needs and liabilities for which these resources are required to provide may be summarised under the following five heads:—

(i) A working balance in India for (a) the current expenditure on revenue and capital account of the Imperial and Provincial Governments throughout India, (b) the expenditure of local boards and municipalities for which the Central Government act as banker, (c) The Government savings banks, and (d) miscellaneous funds and services such as funds in court.

(ii) A working balance in the United Kingdom for the “ Home Charges ” of the Government of India on revenue and capital account, including the capital outlay of most of the Indian Railway system.

(iii) A reserve fund for the maintenance at the par of 1 s. 4 d. per rupee of the exchange value of the rupee with the sovereign.

(iv) A fund for securing the convertibility of the notes of the Government of India.

(v) The provision in India of fresh supplies of coined rupees and of sovereigns...at the rate of one sovereign per 15 rupees. In addition, the system.....is used to provide facilities for remittance to India by means of Council Bills and Telegraphic Transfers of such sums as may be required to meet the balance of trade in India's favour. This use of Indian balances is limited only by the amount of resources available in India to meet the sales, subject, however, to the notification that Bills will be sold indefinitely at 1 s. 4 $\frac{1}{2}$ d. per rupee.”

§ 25. Council Drafts System :—The system of Reverse Councils and Council Bills is an important part of the Gold Exchange Standard system, especially as it was worked during the pre-War period. Government, however, have never bound themselves by law to sell Reverse Councils or sterling bills, and, moreover, occasions for selling them have been comparatively rare. But, as we have already seen, the system of Council Drafts (Council Bills and Telegraphic Transfers) has been the

fly-wheel of the machinery for the management of Indian currency, exchange, and finance. In tracing the history of the Indian currency system till the eve of the War, we have made frequent reference to the sales of Council Bills, but in spite of some repetition it may be useful to give a connected account of the origin and development of the system and explain its mechanism more fully here.*

The practice of drawing funds from India by the sale of bills of exchange on India dated from the time of the East India Company. Up to 1893, however, the sale of Council Drafts[¶] was as a rule limited by the actual requirements of the Secretary of State for meeting the Home Charges. The system was both effective and profitable to the Indian Government, because it enabled the Secretary of State to obtain funds at as favourable a rate as possible. It was also convenient to trade in providing a ready means of settling a large part of debts due to India from foreigners on account of India's surplus of exports over imports. In fact it was the existence of this surplus in normal times which made the system of Council Drafts possible and profitable.

For some years after 1893, a negative use, so to say, was made of the system for forcing up the exchange value of the rupee by a temporary cessation of the sale of Council Drafts. This had the effect of making the rupee less freely available and tended to raise its price in terms of sterling.

We have already seen how in 1898 after the rupee had at last risen to 1 s. 4 d., Act II of 1898 authorised the sale of Council Drafts against gold set aside at the Bank of England as part of the Indian Paper Currency Reserve, and notes of corresponding value were issued in India to meet the Council Drafts. The object was not merely to draw funds from India to meet the Home Charges but quickly to expand the currency in times of monetary stringency in India, as an alternative to the

* The following account is slightly abridged from the Chamberlain Commission's Report, paras 170-176.

¶ Council Drafts is a generic term including Council Bills and Telegraphic Transfers,

shipment of sovereigns to India on private account, when the Government of India had no surplus treasury balances with which to meet Council Drafts.

A further step was taken when gold accumulated in London and representing the proceeds of the sale of Council Drafts against the issue of notes in India was regarded as available for the purchase of silver for coinage in India. Since 1904, as already seen, an offer to sell Council Bills was kept standing. A similar train of events resulted in the issue by the Secretary of State, as occasion required, of notifications offering to sell Council Drafts against sovereigns in transit from Australia, or Egypt to India, the motive being to avoid the expense and the waste involved in the shipment of sovereigns first to India and then to London for the purchase of silver, sovereigns beyond a particular limit not being required in India.

In 1909 and 1910, Council Drafts were freely sold to obtain gold in London in place of the large quantities of rupees, which had accumulated in the Gold Standard Reserve in India through the sale of Reverse Councils in London during the crisis. The effect of this was to bring the Gold Standard Reserve Fund back to London.

Profits on the mintage of rupees, which necessarily first took the form of rupees, were converted into sterling in London, the rupees which represented the profits being issued in India to meet the Council Drafts sold in London.

The considerations affecting Council Drafts thus came to be very much wider than the mere question of putting the Secretary of State in funds for paying the Home Charges. To this purpose was added that of securing the convenience of trade and that of so manipulating the disposition and location of the resources of Government as to give the fullest effect to Government policy in matters of currency, exchange and finance.

Before concluding this account a description may be given of the procedure adopted in selling the Council Drafts.

Whenever there is a demand for remittance to India and money is wanted for any purpose by the Secretary of State, on

each Wednesday an announcement is made as to the total amount for which the Council Bills and Telegraphic Transfers (for which the rate is ordinarily higher by $\frac{1}{32}$ d. per rupee than that for the bills) are to be sold the next Wednesday. Tenders are invited from intending purchasers and allotment is made to the highest bidder, subject to a minimum price. On intermediate days, Intermediate or Special Bills are made available at a somewhat higher rate, the exact rate and the maximum amount of such "Intermediates" being fixed for the week each Wednesday.

The arrangements made each Wednesday are laid before the next meeting of the Finance Committee of the India Council and subsequently before the Council itself for approval.*

§ 26 Effects of War on the Indian Currency†:—The effects might be considered under two main periods. (1) The first period extends from the outbreak of the War in 1914 August to 1915 autumn. This was a period of dislocation involving a general weakening of the currency and exchange position.

(2) The second period falls between 1915 autumn to the end of 1919. This may be considered as a period of revival and was characterized by great vigour in production. It witnessed a very large rise in the exchange and an unprecedented rise in the gold price of silver, which was particularly pronounced towards the end of the period.

§ 27. First Period: (1914 August to 1915 autumn):—The outbreak of the War dealt a rude shock to public confidence and caused a general dislocation of trade and business. The principal symptoms of this were a weakening of the exchange, withdrawals of Savings Bank deposits, a demand for the encashment of notes; and a run on the Indian gold stocks. Government met the situation by prompt measures which helped the early restoration of confidence. The weakening of the exchange was met

* The recently started practice of Government purchase of sterling constitutes an important modification of the system described above and is discussed later on.

† This account is largely based upon the Report of the Babington Smith Committee, 1920.

by offering sterling drafts or Reverse Councils, which were sold to the extent of about £ 8 millions up to the February of 1915, when the demand for Council Bills revived, and apart from short spells of weakness, Indian exchange remained strong throughout the second period, there being a very large demand for Council Bills the whole of which could not be met.

A large amount—Rs. 6 crores out of a total of $24\frac{1}{2}$ crores—was withdrawn from the Savings Bank deposits in the first two months of the War. The net withdrawals amounted to Rs. 8 crores till the tide turned in 1915-16. The demands were freely met, and this proved useful in restoring confidence and attracting back the deposits, which again rose to Rs. 18 crores by the end of 1918-19 (i. e. $6\frac{1}{2}$ crores less than the original amount.)

The demand for the encashment of notes was also freely met, notes of the value of 10 crores being returned to the Treasuries up to March 1915. But from that time onwards there was a steady increase of the note circulation.

Lastly, there was a run on the Indian gold stock which took the form of a keen demand for gold in exchange for notes. Precautions against the internal use of the gold so acquired proving useless, the issue of gold to private persons was altogether stopped, and notes were paid after that in silver coin only.

All these embarrassing symptoms disappeared by the end of the first period. Government on the whole may be said to have faced the currency and exchange situation boldly and successfully. Public confidence was restored by the assurance given to the banking and commercial community of adequate and continuous facilities for remittance abroad and by the readiness with which Government encashed currency notes as they were presented.

§ 27 The Second Period;—(1915 autumn to the end of 1919):—

After the first shock of the War had passed away, the Currency mechanism worked smoothly for some time, and it was not till the end of 1916 that acute complications arose. There was a rapid rise in the price of silver and an increasing difficulty of obtaining it to meet the heavy demands for silver coins in India.

In the first place there was a heavy excess of exports over imports, and the balance of trade which was at the outset of the War unfavourable to India, became now embarrassingly favourable. Although the export trade suffered on account of the War, it made a steady recovery thanks to the insistent demand for India's exports on the part of the Allies for the prosecution of the War. The import trade, on the other hand, suffered more, as we have already seen. * The result was that there remained a large excess of exports over imports to be liquidated.

To make the situation still more difficult the Government of India had to incur heavy (recoverable) expenditure on behalf of His Majesty's Government. From 1914 to December 1919, £ 240 millions had to be so spent on military equipment in the Eastern theatres of the War and for meeting civil expenditure in occupied territory. In addition to this, arrangements had to be made for the financing of purchases in India, on behalf of some of the Dominions and Colonies and also for the African importers of Indian produce.

The combined effect of these factors was to create a heavy demand for Indian currency. The decrease in the imports of precious metals on account of the restrictions placed on their export by foreign Governments further added to the ticklishness of the situation. As the pre-War methods of liquidating the favourable balance were not available, Government had to provide some sort of a substitute to prevent the paralysis of the export trade so vitally necessary for the successful prosecution of the War. They had, therefore, to sell Council Bills in London on a very large scale by way of providing means of remittance to Indian exports. To meet these Bills it became necessary to undertake extensive coinage of rupees. This was a task which presented almost insuperable difficulties as various circumstances conspired to send up the price of silver to undreamt-of heights.

There was a great shortage of the supply of the white metal as compared with its pre-War level of production, owing

* See pp. 271-274, vol II, above.

to internal disturbances in Mexico and the great increase in the cost of production.

On the other hand, there was an unusually keen world demand for the metal (mainly for currency) on account of the shortage of gold and the almost universal anxiety on the part of belligerent and neutral governments to conserve their supplies of it. The heaviest demand came from India and China. We have already seen that the burden of liquidating the favourable balance of trade and finding purchasing power for the expenditure on behalf of the British War Office was mainly thrown on the Government of India and took the form of large demands for the local currency, especially for rupees. The demand was further accentuated by the melting of rupees (notwithstanding its prohibition by law), when the intrinsic value of the coin exceeded its face value in the course of the great rise in the price of silver.

Another factor which operated in the same direction was the influence of the dollar-sterling or the New York-London Exchange. When it showed a tendency to move against England, it was "pegged" or fixed by the action taken by both * the Governments at £ 4.76: \$1. It was essential to do this for maintaining smooth trading relations between the two Allies in the Great War. The movement of the dollar exchange against England was caused by England's excess of debits over credits in relation to America, and secondly, by the practical suspension of the gold standard in England and the inflationary character of a virtually inconvertible paper currency with which the country was flooded. As a result of this a distinction between gold and the pound sterling or, more briefly, between gold and sterling came to be established, the pound sterling being depreciated in terms of the American Gold Dollar which was on an effective gold basis. When in March 1919 the sterling-dollar exchange was decontrolled, it made a further move against England, in response to economic forces which were now left unfettered, reaching eventually as low a limit as 3.40 : £1 sterling. †

† The Pre-War parity of this exchange was \$ 4.86: £ 1.

Now the chief payment for silver purchased for India by the Secretary of State had to be made to America in terms of dollars, and the progressive depreciation of the sterling raised the London sterling price and was bound to raise the rupee price of silver also, unless the rupee was given a correspondingly higher sterling value.

§ 28. Rise in the price of Silver:—Having explained the causes of the rise of silver, let us now follow its meteoric flight. In 1915 the highest price of silver was 27 pence per ounce. In 1916, a maximum of 37 pence was reached. In 1917, August, it exceeded 43 pence per ounce (which is the bullion par of the rupee, i. e., a price at which the exchange value of the rupee at 1 s. 4 d. is equivalent to its bullion or intrinsic value.) In September 1917 the price rose to 55 pence. The United States, Great Britain and Canada, however, came to the rescue, all of them instituting a control over the trade in silver and prohibiting its export except under a license and later on except at a specified price. These measures resulted in the price of silver being kept within the limits of 41 and 49 pence per ounce. But in 1919, May, the United States and the United Kingdom withdrew this control and a further rise in the price of silver occurred. In the same month, it reached 58 pence per ounce, after which it continued its upward career throughout the year, reaching the level of 78 pence in December. The highest point was attained in February 1920 when the London quotation was 89 pence per ounce.

§ 29. Measures taken by Government;—We now proceed to describe the measures taken by Government.

(a) *Government control of exchange*:—After the country had lived down the first shock of the War, the demand for Council Bills revived with the revival of the export trade. It was fairly normal till October 1916 after which it rapidly increased owing to the rising favourable balance which, we saw, could not be liquidated by the normal method of free imports of specie. This resulted in the depletion of the rupee reserves in India, endangering the convertibility of the notes. In December 1916, therefore, restrictions were imposed on the sale of Council Bills and the sale of

Intermediate Councils was stopped with the result that there was a divergence between the market rate of exchange and the Government rate. This was detrimental to the export trade which it was essential to maintain uninterrupted for the successful conduct of the War. Therefore, certain measures of control were instituted by the Government, exchange being fixed at 1 s. 4½ d. in January 1917. The sale of Council Bills was confined to some selected Banks and firms, and these were required to do business with third parties at the prescribed rates applying their resources mainly to certain selected articles of exports of importance to the Allies. With the co-operation of the Banks assisted by these control measures, further fluctuations in the exchange were prevented for some time.

(b) *Raising of Exchange Rate*:—Very soon, however, it was found that these measures were not of substantial use in maintaining exchange stability owing to the remarkable rise in the price of silver on which we have dwelt above. Government could not go on selling rupees to the public at 16 pence when the cost of manufacturing a rupee became 18 pence and 20 pence and so on, with the successive rise in price of silver. Government did not entertain the suggestion made by some people in India that this loss should be debited to the Gold Standard Reserve, since it was meant for the very purpose of maintaining exchange stability. Government denied that the Reserve was intended for the use in question and determined to shift this loss on to those who wanted rupees from them.

In pursuance of this policy exchange was raised to 1 s. 5 d. in August 1917, and shortly afterwards the Secretary of State announced his intention to base the rates of exchange on the sterling price of silver raising them as the latter rose.* The result is shown in the following figures:—

† " This announcement was equivalent to declaring the restoration of the silver standard in India like the one that was in existence before 1873. From 1873 to 1893, the measure of value in India was fluctuating with changes in the gold price of silver. The gold price of 165 grains of silver at any moment was the measure of value for the exchange of goods in India. The same was true now in view of the conditions described above..."
Vakil and Muranjan : op. cit., p. 112.

Changes in the Rates of Exchange.

	s.	d.	
3rd January 1917	1	4½	} Sterling
28th August 1917	1	5	
12th April 1918	1	6	
13th May 1919	1	8	
12th August 1919	1	10	
15th September 1919	2	0	
22nd November 1919	2	2	
12th December 1919	2	4	}

The market rate and, later on, the rate for the sale of the Reverse Councils, when these were sold from February 1920 onwards were in the period from January to March 1920, 2s. 6d. 2 s. 8 d., 2 s. 10 d. and 2 s. 11 d. the highest rate being reached in the early months of 1920.

(c) *Purchase of Silver*:—Special measures had to be taken to increase the supply of currency, silver being purchased for the purpose from February 1916. To remove competition from private purchasers in India, Government prohibited the import of silver on private account from September 1917. In 1918, as the result of negotiations with the Government of the United States, the latter passed the Pittman Act which authorised the sale of the silver in the reserve. The Government of India thus purchased 200 million ounces of pure silver at 101½ cents per ounce fine.

(.d) *Conservation and Economy of Silver*:—Further measures were taken for the conservation and economy of silver. Currency legislation was passed in 1917, June, prohibiting the melting and export of gold and silver coins. Notes of the denomination of 1 and 2½ rupees were issued in December, 1917. In January 1918, for the first time nickel coins of the denomination of 2 annas, 4 annas and 8 annas were issued being legal tender up to one rupee. From June 1917, Government purchased compulsorily gold imported on private account at a price based on the sterling exchange value of the rupee, irrespective of the premium on gold. Notes were issued against gold so acquired and gold Mohurs and sovereigns were coined and issued as currency to supplement the silver currency. When the restrictions on

the export of gold from America were removed in June 1919 and the gold markets of South Africa and Australia became free. More gold was imported into the country and acquired by the Government. To encourage its import Government raised the acquisition price so as to include the premium on gold as compared with sterling. Gold so obtained was sold to the public fortnightly from August 1919 with the object of lowering the premium on it.

(e) *Inflation of paper currency*:—Relief was also sought in an increase of the note issue without the usual metallic backing. Further, restrictions were placed on its convertibility such as suspension of the extra-legal facilities for conversion. Another remedy, resorted to was a limitation of daily issues of rupees to single tenderers of notes.

(f) *Financial measures*:—In addition to these, certain financial measures were adopted. The ordinary and the capital expenditure were kept as low as possible and additional taxation was imposed to increase the purchasing power of Government. Further, large rupee loans were floated in India bringing in Rs. 130 crores in 3 years, (1917, 1918 and 1919)—a phenomenal figure as compared with the pre-War figures and expectations. Short-term Treasury Bills from 3 to 12 months were also issued in considerable quantities from October 1917.

All these measures materially assisted the meeting of the heavy demands for remittances to India and the direct demands for currency there.

§ 30. The Babington Smith Committee:—The War had broken out while yet the recommendations of the Chamberlain Commission were under consideration, and, as we have just seen, the events of the War years had raised a crop of fresh problems and new difficulties. The Secretary of State, therefore, decided to appoint another expert committee under the presidency of Sir Henry Babington Smith with the following terms of reference: "To examine the effects of War on the Indian Exchange and Currency system and practice and upon the position of the note

issue and to consider whether, in the light of this experience and the possible future variations in the price of silver, modifications of the system or practice may be required, to make recommendations as to such modifications and generally as to the policy to be pursued with a view to meeting the requirements of trade, to maintain a satisfactory monetary circulation and to ensure a stable Gold Exchange Standard. **

§ 31. Importance of Stability and Means of attaining it:—As the Smith Committee remark "For the current operations of trade, stability (of exchange) is an important facility rather than an essential condition." But the evils of instability are intensified if the movements of exchange are brought about not by economic causes, but by administrative acts. The possibility of official intervention makes it difficult for the commercial community to provide against the risks of fluctuation. Stability of exchange, therefore, is particularly important in an unautomatic currency system like that of India. The Committee considered at first certain proposals which aimed at attaining stability at the old level of 1s. 4 d.

One of these proposals was to reduce the fineness or the weight of the rupee so as to fix the exchange value at the old level and still maintain the token character of the rupee, however high the price of silver might rise. This was turned down by the Committee on the ground that the credit of the Government would be impaired by such a step. Gresham's law would come into operation so that the old full-weight rupees would disappear from circulation, and that on the whole the social and economic consequences would be undesirable.

* The last phrase of the reference under which the Committee were directed to make recommendations with a view "to ensuring a stable gold exchange standard" was interpreted by the Committee as precluding them from the consideration of the question of a return to the silver standard or the introduction of a bimetallic standard. The Committee do not, however, say anything about the gold standard, and we are left to speculate whether this was because they regarded the gold standard as even more unthinkable than silver monometallism or bimetallism, or because they were anxious not to touch what was a sore point with many, or again, because they implicitly accepted the view sedulously propagated by some of the advocates of the gold exchange standard that it was practically and essentially indistinguishable from the gold standard.

Another proposal was that a two-rupee or three-rupee silver coin of lower proportional silver content than the rupee should be issued with the intention that it should circulate side by side with the existing rupee, the coinage of which would be temporarily suspended. The Committee rejected this proposal as being open to many of the objections to the first proposal and adduced, as a further reason against it, that these units would be too large for the bulk of retail transactions in India.

For similar reasons they opposed the suggestion in favour of nickel rupees.

Lastly, the proposal to introduce complete or partial inconvertibility of the note issue so long as the price of silver continued high also failed to commend itself to them. They feared that it would impair the credit of Government and destroy popular confidence, as the note-using habit was as yet too little established in India to render the introduction of such a measure possible without grave risks.

§ 32. Recommendations—The question whether the exchange should be stabilised at the old level or somewhere near the new level which it had reached, was decided by the Committee in favour of the latter alternative, on the ground that it would shorten the period of uncertainty and prevent economic dislocation and social discontent (See. § 33 below). The following is a summary* of the main recommendations of the Committee.

(a) That the rupee, unchanged in weight and fineness should remain unlimited legal tender.

(b) That the rupee should have a fixed exchange value and that this exchange value should be expressed in terms of gold at the rate of one rupee for 11.30016 grains of fine gold *i. e.*, one-tenth of the gold contents of the sovereign.

(c) That the sovereign previously rated by law, at Rs. 15 should be made legal tender in India at the revised ratio of rupees ten to one sovereign.

* The summary has been taken from Appendix 3 to the Report of the Hilton Young Commission on Indian Currency, 1925-26, but the recommendations with regard to the constitution and location of the Paper Currency Reserve have been omitted.

(d) That the import and export of gold into and from India should be freed from Government control as soon as the change in the statutory rate to Rs. 10 had been effected and that a Gold Mint at Bombay should be opened for the coinage into sovereigns of gold tendered by the public.

(e) That the notification of Government undertaking to give rupees for sovereigns should be withdrawn.

(f) " That the prohibition of the private import and export of silver should be removed and that the import duty on silver should be repealed unless the fiscal position demanded its retention.

(g) That the Gold Standard Reserve should contain a considerable proportion of gold and the aim should be to hold the remainder of the reserve in securities issued by Governments within the British Empire (other than the Government of India) maturing within twelve months. A portion of the gold held in the Reserve, not exceeding one-half, should be held in India.

The recommendation to fix the exchange value of the rupee at 2 s. gold was qualified by the following remarks:—

" If, contrary to expectation, a great and repaid fall in world prices were to take place and if the costs of production in India fail to adjust themselves with equal rapidity to the lower level of prices, then it might be necessary to consider the problem afresh ".

§ 33 The Committee's Case for the high rate:—The principal reason for the high rate recommended by the Committee was their expectation, that for a long time to come, the price of silver would continue to be high, and they thought that, if the exchange value of the rupee was fixed at a figure not lower than 2s. gold, the rupee would be once more established as a token coin, and the maintenance of a satisfactory monetary circulation would be assured.

A consideration of the general economic effects of a high rate of exchange also led them to prefer it. A low rate would mean high prices which would entail great hardships on the

poorer classes and on those who had fixed incomes, and would promote great unrest and discontent.*

As regards the effect of the high rate on the trade of India, the Committee expressed the view that, although it stimulated imports and discouraged exports, these effects were transitory in character and would disappear when wages and other elements of cost had adjusted themselves to the new rate of exchange. The export trade was also likely to suffer less than was feared by some people, because the demand for Indian goods abroad was very keen owing to the world shortage of raw materials and food stuffs. Besides, the high rate of exchange and the general cheapening of the imports would bring substantial advantages to the Indian producer. It would tend to keep down the cost of imported stores and machinery in terms of rupees, and by reducing the cost of living in India it would lower wages or at least check their further advance.

Lastly, Government finances would stand to gain enormously from the high level of exchange and the annual saving in respect of the sterling obligations would amount to rupees 12½ crores, if the old ratio of 1 s. 4 d. was abandoned in favour of the new one of 2 s. gold. There would of course be a loss involved in the revaluation in terms of rupees of the sterling investments and of the gold in London. But the whole of this loss would be wiped out in the course of three years by the savings effected in connection with the Home Charges. And after this has been done, a considerable surplus revenue would remain and would be available for employment in further economic development of the country or in reducing taxation.

* "These views are not a matter of theory alone. Disturbances have actually arisen in various parts of country from time to time as a result of high prices, and the social and economic discontent to which they gave rise is especially serious in a country where the mass of the population is ignorant and uneducated, and inclined to attribute all calamities to the action of the Government. The rise in prices in India has now reached a point at which it is injurious to the country as a whole, and we believe that any measures tending either to reduce prices or to check a further increase would be beneficial to the mass of the population." See Report, para. 48.

§ 34. Gold or Sterling?—In support of their conclusion that the rupee should be fixed in relation to gold rather than with sterling, the Committee adopted the following line of argument:*

The main inducement for retaining the fixed relation with sterling was that a larger part of India's trade was with sterling-using countries than with countries upon an effective gold basis, like the United States. The sterling-using countries happened to be also those included in the British Empire, so that an exchange system on a sterling basis would not only be convenient to trade, but would also promote trade within the Empire rather than outside it, and further retain for centres within the British Empire the finance of Indian trade.

While this consideration had undoubtedly some weight, the Committee did not consider that a fluctuating sterling exchange would create an obstacle of a serious character to trade between the United Kingdom and India or to existing methods of financing that trade, provided that the system already in force was such as to enable trade requirements for remittance to be met readily as to their full amount. In any case, the fluctuations of the rupee-sterling exchange would only last until the gold basis of the British currency was restored.

On the other hand, by being linked with sterling the rupee was bound to share in the progressive depreciation of sterling. There is no reason why India should suffer this inconvenience, especially, as owing to her position as an exporting country with a favourable trade balance, she could easily avoid it by linking her currency to gold.

Further, it was very desirable to stabilise the rupee as early as possible at a level which would ensure its remaining a token coin, and would remove the necessity for further increases in its value to meet successive rises in the sterling price of silver, which were likely to result from a progressive depreciation of sterling. This consideration made it difficult to fix the sterling value of the rupee with any confidence of being able to maintain it. If, however, the rupee was linked to gold and not to sterling, one disturbing cause at least would be eliminated, since any rise in the

* See Report, paras 55-57.

sterling price of silver would be counterbalanced by a similar automatic rise in the sterling value of the rupee.

In any case, the sterling value for the rupee—if it was decided to fix the rupee in relation to sterling—would have to be very high, and it would be found too high, if, in course of time, sterling became once more equivalent to gold. This would necessitate another change in the ratio by Government intervention, and would be injurious to commercial confidence. If, on the other hand, the value was fixed in relation to gold, it could safely be fixed at a lower figure. The sterling equivalent, although, to begin with, it would fall in correspondence to any recovery in sterling, would ultimately coincide with the gold value.

Moreover, if the rupee and the sovereign were both to remain legal tender in India and available for circulation, it was necessary that the relation of the rupee with the sovereign should be fixed, since two coins cannot remain in circulation and at the same time stand in variable relation to one another. The result would be that the relation of the sovereign to gold would vary, in fact that the sovereign would become a token coin in India divorced from its bullion value, and rated at a fixed number of rupees. It would follow that the import of sovereigns by the public would have to be prohibited with the attendant danger of smuggling and illicit coining and that gold coin and bullion would not be interchangeable.

§ 35 Mr. Dalal's Minute of Dissent:—Mr. Dadiba Merwanjee Dalal wrote a stimulating and spirited Minute of Dissent differing from his colleagues in practically all their conclusions and strongly condemning recent Government policy in currency, as well as the Gold Exchange Standard system in general.

With reference to Government's action in raising the rate of exchange in response to the rise in the price of silver, he refused to believe that the professed reason for this was the true or the only reason; because apparently Government intended to maintain the rate at a higher level even if the price of silver should fall. In his opinion the rise in the price of silver, which was advanced as a justification for their

action by Government, could have been prevented by removing the embargo on the export of silver after the War had ended, and it was after the War that the greater part of the rise in exchange was brought into force. India could easily have spared the silver for export; such exports would have been profitable to her, and they could have prevented the great rise in the price of silver. It was mainly because the export of silver from India was prohibited, and India was made a potential buyer instead of a seller, that the silver markets were inflamed and the price was raised.

Mr. Dalal was entirely opposed to the rise in the rate of exchange, because he thought its consequences to India would be disastrous. They would seriously disturb the relations between creditor and debtor, cause dislocation and a set-back to several Indian industries and vast continuous losses on the exports of Indian produce, and turn India's balance of trade against her. A fixed high level of exchange would also cause enormous losses in the rupee value of the invested reserves in sterling securities and of gold held as part of the metallic reserves against the note issue. Further, if the sovereigns held by the public were to be redeemed at the statutory rate of Rs. 15 to the sovereign, this would further entail a colossal loss.

An alteration of the ratio is at all times highly objectionable. The legal standard for money payments should be, and usually is, regarded as less open to repeal or modification than perhaps any other legislative act. It gives the people rights as to the kind of money they may demand in exchange for their labour or goods, rights which cannot be removed or modified without inflicting widespread injury and risking the gravest discontent.

Under the stress of the War, money standards were no doubt treated as of little account and there was extensive resort in most countries to inflation as a means of public finance. This however did not apply to India. The inflation of the Indian currency during the War was a genuine inflation as opposed to the artificial inflation in most of the belligerent countries. It arose from the balance of indebtedness due to India. It was caused by the acceptance in London of payments due to India

in the form of sterling, which could not be transmitted to India by the usual means. The commitments to India of the belligerent nations, as to other countries, could not be met in the usual manner through exchange operations or specie remittances.

Unfortunately, India had not been prepared financially for absorbing her favourable trade balances in any other form than the precious metals. There has been no encouragement in India of settling favourable trade balances by investments abroad. This is in fact one of the disadvantages of currency arrangements conducted by Government. During the War, British Government loans could have been successfully floated in India and it was also possible to do something by way of encouraging Indian investors to buy the Indian sterling loans held in London, if arrangements had been made at the Government district treasuries in India.

The break in the standard may have been justifiable during the War, but when the War was over, people's right in the standard money of the country should have been protected from further modification. If the choice was between a certain amount of inconvenience to trade and abandonment of the legal standard, the former alternative should be unhesitatingly chosen. It was for the trade to accommodate itself to the standard rather than the other way about.

The high price of silver was entirely artificial, and the removal of the embargo on its export combined with a refusal to raise the rate of exchange (and so far make the sale of silver unprofitable) would lower it.

But even otherwise Government could meet the situation by stopping the coinage of fresh rupees of which the country had already more than enough, and not selling Council Bills beyond the requirements of the Secretary of State.

Even assuming (without admitting) that only two alternatives were open to Government, viz., raising the rate of exchange and debasing the silver coinage, the latter would be the lesser of the two evils.

There was no advantage in making the rate of exchange follow the price of silver. With the ruling high prices of silver there was no more any economy in using it instead of gold.

Mr. Dalal's offensive against the Gold Exchange Standard system need not be noticed here in detail. His criticisms along with others will find a place in the discussion of the merits and demerits of the system which will be undertaken later on.

§ 36. Government's action on the Report* :—Government accepted the Committee's recommendations and took the following steps to put them into force :—

(i) *Control of Exchange* :—In January 1920 the demand for Council Drafts had ceased and a strong demand for Reverse Councils had set in. During January the drafts had been sold at a rate based on the rate of 2 s. 4 d. which had been fixed for the sale of Council Bills, but in compliance with the Committee's recommendations Government notified that Council Drafts and Telegraphic Transfers would be offered for sale weekly by competitive tender with no fixed minimum rate; and that, in future, Reverse Drafts and Telegraphic Transfers would be offered in India, when occasion so required, at a rate based on the sterling equivalent of the price of 11.30016 grains of fine gold as measured by the prevailing sterling-dollar exchange, less a reduction representing the cost of remitting gold.

(ii) *Change in the legal tender value of the sovereign* :—The internal ratio of one sovereign for Rs. 10 could not be made effective so long as gold bullion continued to command a high premium over the price indicated by the ratio recommended by the Committee. We have already seen how, as far back as 1917, Government had started the compulsory acquisition of gold imported on private account and how they had begun from September 1919 their series of fortnightly sales of gold with a view to reducing the premium on it. Gold, however, still commanded a high premium over the price recommended by the Smith Committee. In February 1920, Government announced that,

* See Appendix 3 Vol. II, Report of the Royal Commission on Indian Currency and Finance, 1925, and also H. Stanley Jevons : *Money, Banking and Exchange in India*, Chap. XV.

during the ensuing six months, a minimum of 15 million *tolas* of fine gold would be sold but this original programme was extended by further sales in August and September. After selling a large quantity at an average rate of rupees 22 per *tola* the gold sales were stopped in October 1920 and the price of gold which had been controlled to some extent by the Government sales again went up. This part of Government's policy, therefore, must be pronounced a failure.

By Ordinance No. III of 21st June, 1920, sovereigns and half-sovereigns ceased to be legal tender in payment or on account, but provision was made for their acceptance by Government at the ratio of Rs. 15 during a moratorium of 21 days, on the expiry of which the restrictions on imports of British gold coin were also withdrawn. The sovereigns and half—sovereigns tendered at the Currency Offices and Treasuries in the 21 days during which the moratorium continued amounted to about £ 2½ millions.

The Currency Committee's recommendation that the sovereign should be made legal tender in India at Rs. 10 instead of Rs. 15 was given effect to by the Indian Coinage (Amendment) Act, No. XXXVI of 1920. This act restored the legal tender character of the sovereign and half-sovereign which had been suspended by Ordinance No. III of 21st June 1920. The rate fixed by the new Act was Rs. 10 to the sovereign, and instructions were accordingly issued to Treasuries and Currency Offices that sovereigns and half-sovereigns if presented should be received at the rate of Rs. 10 and Rs. 5 respectively, but that they should not be issued. As the market price of the sovereign continued to be above Rs. 10, it never functioned as currency at the new ratio. It was therefore thought unnecessary to open a gold mint in Bombay.

(iii) *Abolition of War-time restrictions* :—In February 1920 the prohibition on the import of silver (but not on export) was removed, and also the import duty of four annas per ounce which had been levied was abolished. Similarly the notifications which had been issued prohibiting the use of gold and silver coin otherwise than as currency, or dealing in them at a premium, were also

cancelled. The fall in the price of silver and the return of silver coin from circulation which commenced in May, 1920, made possible the abolition of the remaining War-time restrictions on the movements of precious metals. On the 21st of June the restrictions on the import of gold bullion and foreign coin were removed. Also a few days later restrictions on the use of silver for making payments on behalf of Government were withdrawn and Treasury Officers were instructed that payments should in future be made in the form of currency desired by the payee. At the same time, steps were taken in the direction of renewing the extra-legal facilities (for conversion of notes into rupees) which had been temporarily withdrawn. The Treasury Officers e. g. were instructed as far as possible to give silver in exchange for notes if presented in reasonably small quantities. In short, so far as silver was concerned full effect was given to the recommendations of the Currency Committee before the end of 1920.

The measures taken with reference to the reconstitution of the Paper Currency Reserve will be referred to later on.

§ 37. Sale of Reverse Councils :—We must now recount in greater detail Government's attempt to maintain the new ratio of 2 s. gold and the ghastly failure with which it met. On the date of the publication of the Smith Committee's Report the American cross-rate* had reached the low level of 3.65. It was obvious that the existing rate of the rupee-sterling exchange must rise very considerably, if Government were determined to keep up the value of the rupee at 2 s. gold. Indian exporters under these circumstances were anxious to discount their export bills as quickly as possible in order to save themselves from the expected rise of exchange. But this rush of the exporters to turn their bills into rupees was itself bound to send up the sterling value of the rupee, which, accordingly rose to 2 s. 8½ d. within three days of the announcement of the 2 s. gold ratio. Another fall in the American cross-rate caused a further rise in the rate

* "The rate of exchange between London and New York is spoken of in India as 'the American Cross-rate.' or as the 'New York Cross-rate'. A cross-rate is the rate of exchange between any two places outside of one's own country."

of exchange which stood at the unbelievable figure of 2 s. 10½ d. on February 11. After this, however, a reaction set in. The rush of the exporters to discount their bills had abated. The demand for sterling on the other hand became more and more intense owing to Government's decision about the ratio. Commercial firms and private persons hastened to make their remittances to England, which in ordinary course of things would have waited for several months, in order to take advantage of the abnormally high rate of exchange.

As a result of the huge War-time profits made by certain sections of the people, there was a heavy boom of company flotations, and this meant orders on an unusually large scale for foreign plant and machinery, of which the cost was remitted in advance in order to make the best of the high rate of exchange so long as it lasted. There was also a good deal of speculation in exchange, as it was easy to make handsome profits by the simple process of first turning rupees into sterling when the rate was high, and then translating sterling back into rupees when the exchange came down, as the speculator hoped and anticipated it would.

This heavy demand for sterling, however, made for a rise in its value i. e. a fall in the value of the rupee. The divergence between the market and the official rate which thus arose and which at times amounted to as much as 3 to 4d. further stimulated the demand for the Reverse Councils.

But by far the most important cause responsible for the sagging down of the exchange was the tendency towards the adverse balance of trade referred to above as having commenced in January 1920. This tendency gathered momentum with every month that passed. Government at first started selling Reverse Councils at sterling rates based on 2 s. 8d. on the 5th of February. The rate was raised to 2 s. 10 $\frac{2}{3}$ d. on the 12th of February, but thereafter it decreased as the sterling appreciated. By the end of June, the balance of trade had begun to turn strongly against India, with the result that the market rates of exchange had not merely departed from the parity of gold but had fallen below the parity of 2s. sterling. Government after this tried to

maintain the rate at 2 s. sterling. Consequently at the sale of 24th June and subsequent sales the rate adopted for Immediate Telegraphic Transfers was 1s. 11- $\frac{1}{2}$ d. The reason advanced was that this represented the rate, which would ultimately hold when sterling returned to parity with gold. But in reality it meant that Government had given up hopes of giving effect to the 2 s. gold rate recommended by the Smith Committee, which thus had mounted, shone, evaporated and fallen—all within the brief space of less than six months from the time of its enthronement. The market rate of exchange continued to fall without Government being able to arrest its downward career. They were compelled to reduce their own rates following the market rate, and the only principle that was adopted was to keep the official rate at a somewhat higher level than the market rate. But this could not last indefinitely, and Government finally abandoned their attempt to regulate the exchange. At the end of September 1920, the sales of Reverse Councils since the beginning of the year had amounted to £ 55,382,000. The Reverse councils were paid in London out of the proceeds from the sale of sterling securities and Treasury Bills belonging to the Paper Currency Reserve. These securities and Bills had been bought at the rate of Rs. 15 to the pound, but they were sold at rates ranging from Rs. 7 to Rs. 10. The difference between the selling and buying price measured an aggregate loss of Rs. 40 crores to the Indian exchequer.

Apart from the heavy losses suffered by the Indian exchequer in connection with the sale of the Reverse Councils, the eventual collapse of the exchange was ruinous to business in more ways than one. A very considerable deflation of money had occurred as the result of the sale of the Reverse Councils. The note circulation between the 1st of February and 16th of September had been reduced from Rs. 185 crores to Rs. 158 crores by the progress of cancelling the notes received by Government in payment for the Reverse Councils. This very substantial withdrawal of currency had proved ineffective for maintaining exchange owing to the abnormal activity of the import trade and the absence of any support from exports. But it caused an acute monetary stringency, and was responsible for

a fall in the level of prices. Both these circumstances together greatly enhanced the difficulties of businessmen, who were compelled to sell off their stocks at ruinously low prices.

The heaviest loss, however, was due to the fact that the commercial community had counted on Government maintaining the exchange at the high rate chosen by them. Goods had been ordered under the confident expectation that exchange would remain high, but the exchange had fallen heavily by the time they arrived.

This meant nothing less than bankruptcy to many importers whose reliance on Government's ability to keep the exchange at the desired high level was so complete that they had failed to take the usual precaution of covering their exchange.

§ 38. Government policy examined:—All this, however, may fairly be taken as proving that many sagacious and hard-headed businessmen did not regard the maintenance of the high rate as an impossible task, whatever they may have thought about its advisability.

Government themselves had no doubt in their mind about the practicability of maintaining the ratio at 2 s. gold, being reassured on this point by the majority Report of the Babington Smith Committee. It is true that Mr. Dalal in his able dissenting minute had urged strongly against the high ratio and dwelt at length on the evils sure to follow from it. But he does not seem to have laid any particular emphasis on the *impossibility* of maintaining the ratio for any length of time.

It is, however, a very strange phenomenon that the feeling about the impracticability of maintaining the new ratio was not as common as it might have been expected to be. When Government set out to give effect to the recommendations of the Babington Smith Committee, there were several facts before them which might have given them pause in initiating such a revolutionary change in the currency standard. For example, on August 1920, when the altered ratio was to have to come into effect, gold was selling at Rs. 23½ per *tola*, whereas according to the new ratio the price of gold ought to have been Rs. 15-14-0. In view of such a great disparity it should have been clear that

it would be extraordinarily difficult, if not impossible, to maintain the ratio of 2 s. gold. Again, the price of silver itself had gone down to about 44 d. per ounce and therefore the danger of rupees being melted down had practically disappeared. Moreover, even if a certain amount of melting had taken place this would not have mattered much considering the vast volume of rupees in circulation.*

The Babington Smith Committee had entirely misread the situation when they put the rise of silver in the forefront of causes explaining the rise in Indian exchange. The real cause of rise in the sterling value of the rupee was the greater rise in sterling prices as compared to the rise in rupee prices. According to the Purchasing Power Parity doctrine ¶ the rate of exchange had to move up in sympathy so as to bring about equilibrium. The same doctrine explained the subsequent fall in the exchange which was due to the more rapid decline of world prices (or sterling prices) since 1920 than the Indian prices. This turned the tables against the rupee causing a fall in its sterling value, during and for some years since 1920, before it began to appreciate again and ultimately reached 1 s. 6d.‡. The 2 s. gold rate meant a considerable overvaluation of the rupee in comparison with its purchasing power parity with gold at the time, and the attempt to give a fixed gold value to the rupee was premature, as the value of gold itself was undergoing the most violent variations and the conditions of international trade were still extremely unstable.§

* See Ambedkar, op. cit. p. 207.

¶ This is explained at greater length in the next chapter.

‡ "The rise in the price of silver was really a mere coincidence due to a large extent to speculation. In ignoring the significance of the rapidly altering price-levels and fixing its attention merely upon the speculative prices of silver, lay the fundamental error of the Smith Committee's Report on Indian Currency. In linking the rupee to gold at 2 s., it overlooked the real character of the rise which had taken place and underestimated the deflation which would have become necessary to maintain that rate. Its surmises regarding the probable course of prices in other countries were perhaps the most ridiculous examples of economic prophecy to be met with in history", Vakil and Muranjan : op. cit. pp. 340-41.

§ See Gustav Cassel's Memorandum to the Hilton-Young Commission, Report, Vol III, Appendix 92.

There was no real connection between the rise of the price of silver and the appreciation of the rupee in terms of sterling. In fact the high price of silver was partly the result of the *depreciation* of the rupee as well as of sterling in terms of commodities in general. Even supposing, however, that the rise in the price of silver had been the chief cause of the rise in the exchange the former was largely speculative. The tremendous range of variation in its prices as shown in the following table* should have served as a warning that the rise was without an element of permanence and stability.

Price of Silver in Sterling (Pence) 1

Year	Highest	Lowest	Average	Range of variation
1913	$29\frac{3}{8}$	$25\frac{15}{16}$	$27\frac{9}{16}$	$3\frac{7}{16}$
1914	$27\frac{3}{4}$	$22\frac{1}{8}$	$25\frac{5}{16}$	$5\frac{5}{8}$
1915	$27\frac{1}{4}$	$22\frac{5}{16}$	$23\frac{11}{16}$	$4\frac{15}{16}$
1916	$37\frac{1}{8}$	$26\frac{11}{16}$	$31\frac{5}{16}$	$10\frac{7}{16}$
1917	55	$35\frac{11}{16}$	$40\frac{7}{8}$	$19\frac{11}{16}$
1918	$49\frac{1}{2}$	$42\frac{1}{2}$	$47\frac{9}{16}$	7
1919	$79\frac{1}{8}$	$47\frac{3}{4}$	$57\frac{1}{16}$	$31\frac{3}{8}$
1920	$89\frac{1}{2}$	$38\frac{7}{8}$	$61\frac{7}{16}$	$50\frac{5}{8}$
1921	$43\frac{3}{8}$	$30\frac{5}{8}$	37	$12\frac{3}{4}$

The only defence it was possible for Government to put up was that, having appointed an expert Committee they felt bound to follow its advice, especially as they could not see their way clearly before them owing to the entirely exceptional circumstances then prevailing. But the gravamen of the charge against Government is not that they shaped their policy

* Ambedkar : op cit. p, 204.

in the beginning in accordance with the advice of the Babington Smith Committee, but that having seen the palpable futility of the efforts to make the 2 s. gold rate effective, they still persisted in the sale of Reverse Councils. By the end of June 1920, it was fairly clear that the task which the Government had taken upon themselves was an impossible one, and it would have been a courageous and wise step frankly to have acknowledged defeat at an early stage. As it was, however, Government persevered in their ill-advised attempt to bolster up the exchange, dissipating their huge gold resources in the process and causing tremendous disturbance in the industrial and commercial world. Thus as Sir Stanley Reed put it, "a policy which was avowedly adopted to secure fixity of exchange produced the greatest fluctuations in the exchanges of a solvent country and widespread disturbance of trade, heavy losses to the Government, and brought hundreds of big traders to the verge of bankruptcy."*

§ 39. The policy of Masterly Inactivity (1921-25):— After the failure of the attempt to stabilise exchange, Government had to be content for some time with watching, in a spirit of patient expectancy, the course of events as they unfolded themselves without taking any decisive action.

In the year 1921, the balance of trade was still against India. The depressed condition of the export trade was due to a rapid fall of world prices in terms of gold and the still more rapid fall of sterling prices owing to the steps taken by England to bring sterling back to gold parity. Under these circumstances, the expected happened and the sterling value of the rupee fell steadily. In the course of the year 1921, Government had contracted the currency to the extent of 31 crores and 58 lakhs. This, however, was not enough to arrest the downward course of exchange which was driven to as low a level as 1 s. 3 d. The contraction of currency was continued further in 1921-22 and 1922-23 by the transfer of sterling securities held in London to the Secretary of State's cash balance and by the discharge of Indian Treasury Bills held in the

* Quoted by Dadachanji : *History of Indian Currency and Exchange*, p. 137.

Reserve. With a view to preventing the further fall of the rupee the Secretary of State had also discontinued the sale of Council Drafts.

In 1922-23 the export trade of India showed a revival owing to good harvests and an improvement in the purchasing capacity of the European countries. The joint result of the contraction of currency and the revival of exports was to raise the exchange value of the rupee slowly but steadily. In 1923 September the rupee was equivalent to about 1 s. 3½ d. gold, and the pre-War ratio of 1 s. 4 d. could have been easily restored without adversely affecting any interest whatsoever, as was unsuccessfully urged by the Indian Merchants' Chamber. Government, however, were apparently trying to take the ratio up to 1 s. 6 d., and the rupee as a matter of fact reached the level of 1 s. 6 d. sterling in October, 1924. Government's action after this was directed towards preventing the rise of the rupee much beyond this point. In order to achieve this result the purchases of sterling required for Government remittances and, when necessary, in excess of this, were freely used and fresh currency was issued against these purchases, thus incidentally relieving to some extent the monetary stringency occasioned by Government's policy of deflation. The exchange value of the rupee reached 1 s. 6 d. gold in April 1925, and remained-or, as the critics of Government would like to put it, was held-there since then.

The end of the policy of masterly inactivity was now in sight. The Government of India in response to repeated requests from various quarters promised an enquiry into the currency situation early in 1925 through an authoritative Committee before the end of the year, by which time they anticipated that the world conditions would become sufficiently stable. Later in the year, a Royal Commission on Indian Currency and Exchange was appointed under the presidency of Lt. Commander Hilton-Young.

Before considering the deliberations and decisions of the Commission, we shall turn aside to give an account of the evolution of the Indian Paper Currency system, which perhaps has already been delayed too long.

INDIAN PAPER CURRENCY.

§ 40. Early History :—In 1839 the three Presidency Banks were authorised to issue notes payable to the bearer on demand subject to certain regulations as to maximum issue and reserves. But their circulation was restricted within narrow bounds, being practically confined to the three Presidency Towns. James Wilson, the first Finance Member of India, worked out in 1860 a scheme for a Government Paper Currency and the abolition of the right of note-issue enjoyed by the Presidency Banks. Wilson's scheme contemplated: (a) one-third of the reserve being in cash and the rest in securities; (b) a large number of circles into which the country was to be divided; and (c) a complete divorce between banking and note-issue.

But Sir Charles Wood, the then Secretary of State for India, laid down the following principles on the lines of the English Bank Charter Act of 1844 :

(A) First, that the function of note-issue should be entirely separated from that of banking as was also suggested by Wilson and second, as Sir Charles Wood put it "the amount of notes issued on Government securities should be maintained at a fixed sum, within the limit of the smallest amount which experience has proved to be necessary for the monetary transactions of the country, and that any further amount of notes should be issued on coin or bullion."* Accordingly the Paper Currency Act of 1861 was passed. The country was divided into seven circles of issue viz., Calcutta, Cawnpore, Lahore, Madras, Bombay, Karachi and Rangoon. Notes were issued of the denomination of Rs. 5, 10, 50, 100, 500, 1000 and 10000. They were to be issued without limit in exchange for rupees or British gold coins to the public, and in exchange for gold bullion on the requisition of the Controller of Currency. They were declared unlimited legal tender both at the Government Treasuries and in private transactions but within their respective circle of issue.

A reserve was formed in bullion and coin to the full value of the notes issued with the exception of a certain small portion

* See Keynes : op. cit. p. 39.

invested in the Government of India Rupee Securities as a guarantee of their convertibility.

As to the encashment of notes they could be encashed as of right only at the head office of the circle of issue. At the same time Government Treasuries cashed notes of other circles for bona-fide travellers and for the Railway Companies if they accepted notes of any circle. Payment of dues to Government could be made in the currency notes of any circle.

§ 41. Restrictions as to encashment and legal tender quality of the Notes :—India is a vast country, and conditions of trade cause movements of money from one part of the country to the other at different times of the year. The first use of notes would therefore be for remittance in a more convenient way than by sending specie. Government in this case would have been obliged to send cash from place to place if they had not restricted the legal tender quality of the notes to the circle of issue. If on the other hand, the notes had been made universal legal tender but only encashable at Presidency towns, there would undoubtedly have been a premium on coin at certain times of the year which would have impaired the popularity of the notes.

As it was, however, the Circle System greatly restricted the normal expansion and popularity of notes, and steps were therefore taken from 1903 partially to abolish it. In 1903 the 5-rupee note was made universal legal tender except in Burma, the latter restriction being removed in 1909.

Then in 1910, notes of the denomination of Rs. 10 and 50 were similarly universalised and power was taken to universalise notes of higher denomination by executive order. In 1911, accordingly, the Rs. 100 note was universalised. The Chamberlain Commission recommended the universalisation of the Rs. 500 note also.

Extra-legal facilities for encashment of notes had been provided at the Government treasuries in various places, and the Presidency Banks undertook further to extend such facilities at their Head offices and Branches.

The War period arrested any further development in this direction, as there were difficulties in getting enough rupees coined and the uncovered note issue also increased.

The Babington Smith Committee recommended the abolition of War-time restrictions and further extension of extra-legal facilities for the encashment of notes as essential for making them more popular.

§ 42. Paper Currency Reserve:—Coming to the history of the Paper Currency Reserve, the Act of 1861 provided for a fixed maximum fiduciary issue in the form of Government securities up to 4 crores. This limit was changed from time to time by special Acts to 6 Crores in 1871, in 1892 to 8 Crores, in 1897 to 10 crores; and in 1905 to 12 crores. Up to this time the securities were the rupee securities of the Government of India held in India, but the Act of 1905 authorised the holding of sterling securities in England up to 2 crores. Since 1905, part of the invested portion of the Reserve has thus been in the form of sterling securities.* In 1911, the maximum reserve in securities was fixed at 14 crores, 4 crores of which were to be in sterling securities.

As already pointed out, up to 1898, the whole of the Paper Currency Reserve except a fixed fiduciary portion was held in silver coin in India. In 1898, the Gold Note Act authorised the Government to hold any part of the metallic portion of the Reserve in gold coins. The Act of 1900 gave authority to hold part of this gold coin in London. The Act of 1905 gave full power to Government to hold the metallic portion of the Reserve, or any part of it, either in London or in India, and in gold coin or bullion, or in rupees or silver bullion, with the proviso that all coined rupees were to be held in India only.

As pointed out above, except for a fixed maximum fiduciary issue, which has been raised from time to time, the whole of the rest was held either in gold and silver, bullion and coin. With the gradual expansion of the note issue, an ever diminishing propor-

* See p. 349 above.

tion came to be invested as a result of this practice. On the other hand, a growing proportion came to be held in a liquid form, sometimes as much as 80 to 85%. This was due to a deliberate change of policy and to the use of the liquid part of the Reserve for a new purpose viz., that of supporting exchange whenever necessary. In fact, as we have already seen, this was considered as the first line of defence of the Currency system as a whole.

The result of the policy has been that, although a superlatively safe reserve was held for ensuring the convertibility of the notes, this had been at the cost of economy. This could have been avoided by increasing the invested portion, the best way of doing which was to make cash bear a certain percentage or proportion to the total issue of notes. In this way also the frequent resort to legislature to raise the fiduciary limit could have been avoided.

§ 43. Gross, Net and Active Circulation:—When we speak of the circulation of the Paper Currency, we must be clear as to whether we are referring to the gross, net or active circulation.

(1) By gross circulation is meant the value of all notes that have been issued and have not been paid off. (2) Net circulation is this sum less the value of notes held by Government in its own treasuries. (3) Active circulation is the net circulation reduced by the value of the notes held by the Imperial Bank (and before the Imperial Bank by the Presidency Banks at their Head Offices).

The gross circulation diminishes instead of increasing in the busy season, for then the Presidency Banks and the Reserve Treasuries* (we must now speak of the Imperial Bank instead of the Presidency Banks and the Reserve Treasuries) sent their notes for encashment to the Paper Currency Offices when cash

* In addition to the general system of district treasuries which carry on the daily business on behalf of Government, there used to be 3 Reserve Treasuries established in each of the Presidency towns. Their function was to keep large sums of money for expenditure in case of any serious emergency such as widespread famine or war. The Reserve Treasuries, however, no longer exist. now. See H. Stanley Jevons : op. cit. p. 154.

was required for moving the crops; while during the slack season it was more convenient to hold the reserves in notes. At the same time, however, the active circulation increases showing that notes are used for meeting the seasonal demand side by side with cash.

§ 44. Criticism of the composition of P. C. R.:—The main criticism against the pre-War composition of the Paper Currency Reserve was against (i) the unduly large metallic reserve; (ii) the impossibility of increasing the fixed fiduciary reserve except by a special resort to legislation; and (iii) the holding of and fiduciary or invested reserve or part of it in the form of sterling securities. (i) and (ii) made the system generally inelastic. As regards (iii), the practice was sought to be justified on the ground that the sterling securities were useful for maintaining the exchange value of the rupee and that they possessed the additional advantage of not being liable to depreciation in the event of internal crisis in India.

Under the Indian system, the function of note issue was entirely dissociated from the function of banking and until recently, there was no Central Bank and therefore no Government Banker. There was the Reserve Treasury System, under which Government funds were locked up in their own Treasuries (except for small amounts confided to the Presidency Banks), bringing about a stringency in the money market during the busy seasons of the year.

The internal currency was absolutely inelastic for special and general purposes, and there was no provision for its temporary expansion except by importing funds from abroad either by the purchase of Council Bills or import of sovereigns. Similar defects in other countries have been overcome by the use of deposits and cheques, as in England and America, or by a special and a temporary issue of paper currency against commercial bills of exchange, and lastly by placing Government funds at the disposal of a Central Bank. *

The first method, namely, cheques and deposits is not much in use in India except at the few big commercial centres. The

* See Chapter on Banking.

second has been suggested by the Smith Committee and was accepted. The third has also been adopted by the abolition of the Reserve Treasuries and placing the Government funds with the Imperial Bank of India which now acts as the Government Bank. In order to remedy the general inelasticity due to the first two characteristics of the composition of the Reserve two methods were suggested by the Chamberlain Commission and the Smith Committee respectively. The former recommended that the fiduciary reserve should be fixed at the amount of notes held by Government in the Reserve Treasuries (now abolished) plus one-third of the net circulation. The principle is that the fiduciary issue should not exceed a maximum percentage of the total issue. The Smith Committee suggested that the metallic portion should not fall below a minimum percentage of the total issue; the proportion suggested being 40 per cent, although they held that it would be desirable to maintain a substantial margin above the statutory minimum especially in the busy season. In either case, the fiduciary reserve would increase automatically with the increase of circulation without frequent resort to legislation. The system would thus be more economical and less rigid. As we shall see later on, Government have accepted the Smith Committee's suggestion, although they have adopted a higher percentage for the metallic reserve, viz., 50 per cent.

§ 45. The effect of the War on the Paper Currency:—We saw above how, on the outbreak of the War, there was at the outset a general feeling of panic which led to a severe run on the Paper Currency Offices, notes of the value of 10 crores being returned within the first eight months of the War. As already remarked, however, there was a gradual revival of confidence and a steady increase in the note circulation. The effects of the War on the Paper Currency from March 1915 onwards may be summarised as follows:—

(1) Inflation of paper currency caused by the great demand for currency, which could not all be met by a fresh issue of rupees. The causes of this abnormal demand have already been discussed.

(2) The fiduciary reserve increased tremendously [from Rs. 14 crores (1914) to Rs. 120 crores (1920)] owing to the operation of a series of Acts and Ordinances passed for the purpose, as Government had great difficulty in finding enough coin to be held in the Reserve. Also, recoveries of the War expenditure in India made on behalf of England were made in London by the Secretary of State, and it being considered inadvisable in the Empire interest to hold these proceeds in gold earmarked for the Paper Currency Reserve in London, the alternative of investing them in British Treasury Bills was adopted. As a matter of fact, most of the increase in the fiduciary reserve took the form of British Treasury Bills or short-term sterling securities,* although a part was invested in Indian Treasury Bills as well. (3) The fall in the metallic reserve from 78.9 per cent, in 1914, to 35.8 per cent, in 1919.† (4) The issue of Re.1 and Rs.2½ notes in December 1917 and January 1918 respectively as a measure of economising silver. (5) The abolition of extra-legal facilities‡ for encashment owing to the scarcity of rupees. This resulted in the notes running to a discount of as much as 19 per cent in some places. This applied particularly to the new notes of small denominations. (6) The import of 200 million ounces of American silver released under the Pittman Act to meet the Paper Currency crisis of April 1918.

§ 46. Reconstitution of Paper Currency Reserve:—In September 1919, by the temporary amendment of the Paper Currency Act, the maximum limit to which the currency reserve could be invested was raised to 120 crores, out of which 100 crores had to be British Treasury Bills.

In March 1920, a temporary Act for six months was passed which permitted the retention of the invested portion of the Re-

* The investment in the British Treasury Bills was partly dictated by the consideration that, being short-dated, there was small danger of their depreciating. The other sterling securities, on the other hand, were depreciating to a considerable extent as a result of the War.

† See Table I at the end of the chapter.

‡ As has already been mentioned, these facilities were restored in 1920-21 and have since been extended by the multiplication of the branches of the Imperial Bank which provide for the encashment of notes as a matter of public convenience.

serve at Rs. 120 crores. But it abolished the restrictions as to the locale of the investments and their sterling or rupee character. This proposal was necessitated by the then existing demand for remittances to London and the impossibility of meeting it from the Secretary of State's cash balances. This continued demand was therefore to be met by the disposal of the sterling securities held in the Paper Currency Reserve in London. This, however, involved, under the existing law, the withdrawal and cancellation of currency notes in India to the extent of the rupee value at which the sterling securities were held in the Reserve, i. e., at the rate of Rs. 15 to £ 1.

*Indian Paper Currency Amendment Act of 1920 :—**

In order to place the Paper Currency system on a satisfactory basis in the light of the criticism to which it was subjected by the Chamberlain Commission and the Smith Committee, and the experiences gained during the war, it was felt necessary to pass new legislation to replace the temporary Act of March 1920. Consequently, the Indian Paper Currency Amendment Act became law on 1st October 1920. The provisions of this Act fall under two classes, permanent and transitory.

(a) Permanent provisions:—†

(i) The metallic reserve was to be at least 50 per cent of the total reserve. The reasons for accepting a higher percentage than that suggested by the Smith Committee, which was only 40 per cent, were the necessity of encashing the notes without question in a country like India and the necessity of holding sufficient coin in the Reserve to finance the movements of the crops during the busy season, when notes are generally presented for encashment on a very large scale.

(ii) With the exception of Rs. 20 crores worth of securities held in India, the remainder should be held in England and should be short-term securities not exceeding a period of 12 months as suggested by the Smith Committee.

* This is usually referred to as the Paper Currency Act of 1923, which was a Consolidating Act.

† These provisions were practically identical with the recommendations of the Smith Committee.

(iii) The Controller of Currency was authorised to issue notes up to an amount of 5 crores of rupees against discounted Bills of Exchange maturing within 90 days of their issue.* This extra issue should take the form of a loan to the Imperial Bank which should pay 8 per cent interest to the Government and deposit accepted Bills of Exchange with the latter. (The limit of 5 crores was raised to 12 crores by a subsequent amendment). The provision regarding the 50 per cent statutory metallic reserve was irrespective of this extra issue which was not to be considered for the purpose of fixing the metallic reserve.

(iv) The Secretary of State was not to hold more than five million pounds in gold bullion in London.

(b) Transitory Provisions:—

Owing to the difficulty caused by the necessity of revaluing the gold and the sterling securities of the Reserve on the basis of Rs. 10 to the sovereign instead of Rs. 15, certain transitory provisions became necessary postponing the final attainment of the permanent provisions. With revaluation on the 10 Re basis the metallic portion of the Reserve would have been less than 50 per cent or else it would have been necessary to reduce the circulation which was thought undesirable. It was therefore provided that the invested portion might, for the time being, be fixed at 85 crores.† (The former limit of 120 was now unnecessary, as the circulation had been reduced to some extent by the sale of Reverse Councils met by the sale of sterling securities). Another difficulty was about filling up the gap caused by the revaluation of the gold and sterling securities at two-thirds of their former value. This was easily solved by authorising the Government of India to create rupee-securities of their own hand ('ad hoc' securities,

* The following procedure for the issue of currency notes against bills of exchange was laid down:—

1. No loan shall be made unless the Bank Rate rises to 6 per cent.
2. The entire amount outstanding at any time shall bear interest at the Bank Rate subject to a minimum of 6 per cent for the first four crores and of 7 per cent for the subsequent eight crores.

† As a remedy against monetary stringency, this limit was raised to Rs. 100 crores in 1925, January.

as they were called) and issue them to the Paper Currency Reserve. As these created securities would exceed the limit on rupee securities laid down by the Act, it was provided that the excess should be reduced by gradually replacing them with sterling securities. But as there were no funds available immediately to purchase a large quantity of sterling securities, it was provided that, the interest derived from the securities in the Paper Currency Reserve as by law, and profits on the fresh coinage of rupees, and interest on the Gold Standard Reserve when that exceeded £ 40 millions (which it did on the 30th September 1921), and lastly, interest on commercial bills of exchange deposited with the Controller of Currency as security for the temporary issue should be paid down into the Paper Currency Reserve to reduce such of the created rupee-securities as were above the permissible figure of Rs. 12 crores. The permanent provisions of the Act would thus be eventually carried into effect. On account, however, of the unsatisfactory financial position, Finance Acts of subsequent years allowed these sources of income to be diverted to revenue, except that in 1921-22, the excess in the Gold Standard Reserve was used for the extinction of the 'ad hoc' securities.

On the 1st of April, 1927, the gold and the sterling securities held in the Paper Currency Reserve, which since 1920 had been valued at Rs. 10 to the sovereign, were revalued at the rate of Rs. 13½ to the sovereign in accordance with the provisions of the India Paper Act, 1927, which came into force on that date. The result of this was an increase of Rs. 930 lakhs in the holding of gold and sterling securities, which was set off by cancelling the same amount of Indian Treasury Bills, the holding of which was reduced from 49,77 lakhs to 40, 47 lakhs. *

§ 47. Circulation of Paper Currency and composition of Reserve:—
The following tables show the changes in the composition of the Paper Currency Reserve from time to time since 1914:—

* See Report of Controller of Currency, 1927-28, p. 14.

TABLE I.

	Gross circulation	Securities : Indian and English	Percentage of cash reserve to total circu- lation of notes
	In crores of Rupees		
1914	66.12	14	78.9
1915	61.63	14	77.5
1916	67.73	20	70.5
1917	86.38	48.4	43.9
1918	99.79	61.48	38.4
1919	153.46	98.58	35.8
January 1920	} 186	(a) 87	50.2
March 31st 1920		(b) 120	
1921	} 174	(a) 76	54.0
March 1921		(c) 85	
March 31st 1922	} 174	(a) 71	59.0

N. B —(a. denotes Actual Securities.

(b) denotes Authorised Securities as under the Act of September 1919. Not more than 20 crores out of 120 crores were to be Government of India Securities.

(c) denotes Authorised Securities as provided by the Act of September, 1920.

TABLE II.

Composition of Paper Currency Reserve in recent years.
(Figures in crores of Rupees.)

Year	Gross circulation	Silver coin in India	Gold coin & Bullion	Silver Bullion under coinage	Securities		Internal Bills of Exchange	Percentage of securities.
					Rupee	Sterling		
1925	184.2	70.3	22.3	6.7	57.1	20.0	8.0	40.8
1926	193.3	77.3	22.3	7.7	57.1	29.0	—	44.6
1927	184.1	95.9	22.3	8.5	49.8	5.6	2.0	31.1
1928	184.9	98.7	29.8	7.7	38.0	3.8	7.0	26.4

CHAPTER IX

CURRENCY AND EXCHANGE (Continued)

Hilton-Young Commission at Work.

The Report of the Hilton-Young Commission was published on the 4th of August, 1926. The recommendations of the Commission fall conveniently under the following three heads (i) Choice of a Monetary Standard; (ii) The Ratio of the Stabilisation of the Rupee; and (iii) Creation of a Reserve or Central Bank of India.

§ 1. Defects of the Gold Exchange Standard :—Before propounding their own scheme of a monetary standard for India, the Commission indicate the following defects* of the system as it existed :—

(1) The system was far from simple, and the basis of the stability of the rupee not readily intelligible to the uninstructed public. The currency consisted of two tokens, rupees and rupee-notes, in circulation, with the unnecessary excrescence of a third full-value coin (sovereign), which did not circulate at all. One form of token currency (rupees), into which there was an unlimited obligation to convert the other (rupee notes), was highly expensive and was liable to vanish if the price of silver rose above a certain level, when it ceased to be a token coin.

(2) There was a cumbrous duplication of the reserves, viz., the Gold Standard and Paper Currency and Banking Reserves, with an antiquated and dangerous division of responsibility for the control of currency and credit policy, which in other countries is centralised in and fixed upon a Central Bank. In India, Government controlled the currency, and the credit situation was controlled, so far as it was controlled at all, by the Imperial Bank.

(3) The system did not secure an automatic expansion and contraction of currency. Such movements were too wholly

* See Report, para 21.

dependent on the will of the currency authority, i.e., Government. The system did not automatically enforce contraction of internal currency concurrently with the depletion of the Reserves.*

Similarly, with regard to expansion, on occasions the obligation to buy sterling had been discharged by the Government without any corresponding expansion of currency. The purchases had in the first instance been made against Treasury balances and the currency expansion had been left to be effected at the discretion of the Government.†

This must be regarded as a notable admission, in which Government apparently joined; for it meant the surrender of one of the main defences of the Gold Exchange Standard. Mr. J. M. Keynes, for example, had claimed for the Indian system that it was as automatic as any other and that the only discretion exercised by the Government was in the following two respects:—

- (A) That they kept certain reserves of coined rupees in advance, and
- (B) that by refusing to sell Council Bills they could only exchange the character of the demand and postpone it for a short time, or insist on sovereigns being sent to India where they would be converted into rupees by Government.

* As Mr Denning, the Controller of Currency, points out in his Memorandum to the Commission, the provision for the automatic contraction of currency was particularly defective. "In so far as the sterling value of the Reverse Councils sold was obtained by realising sterling securities in the Paper Currency Reserve, the currency was contracted, but Government could arrange, by borrowing from the Gold Standard Reserve, to meet sterling payments on account of Reverse Councils, without affecting the amount of currency in circulation." See Appendix 5, Currency Comm. Report.

† Regarding the basis of the stability of the rupee, Mr. Denning writes: "The system did not provide for the automatic stabilisation of the rupee. The legal obligation to give rupees in exchange for sovereigns would have prevented the rate of exchange rising above the upper gold point, even if the Government had not been prepared to meet fully the demand for Council Bills at 1 s. 4 $\frac{1}{2}$ d., but there was no statutory safeguard against a fall in the rate of exchange below the lower gold point. In practice, such a fall in the rate of exchange was prevented by the sale of Reverse Councils, but Government were under no statutory obligation to take such action." See Appendix 4.

Ever since the time of the Chamberlain Commission Government had come to look upon this argument as an effective answer to the critics of the Gold Exchange Standard but they had now executed a complete *volte face*, and were prepared to admit as readily as anybody else that its unautomatic character was one of the most serious defects of the system.

(4) Lastly, the Commission pointed out that the system lacked elasticity. The utility of the provision for elasticity made on the recommendation of the Smith Committee was affected by the methods of financing Indian trade. These are based on a system of cash credits or the advance of money against demand promissory notes. There is, therefore, a shortage of genuine inland trade bills as cover against the seasonal increase. Government had, therefore, to announce in 1924, September, that as far as might be necessary, they would use their powers to issue currency against Treasury Bills deposited in the Paper Currency Reserve in London.

These imperfections of the system created a large measure of distrust which had been intensified by leaving too much to executive action and the absence of statutory regulation of the duties of Government as the currency authority. A substantial measure of stability had been attained in the past. But what was lacking was that certainty and simplicity which were essential under Indian conditions to ensure confidence in the stability of the currency and to wean the uninstructed public from the uneconomic habits of hoarding and the disinclination to investment. (Para 22)*

§ 2. Proposals for reform:—The Commission then examined certain alternative proposals for reform, viz., (i) the perfection of the Sterling Exchange Standard; (ii) the adoption of a Gold

* Sir James Begbie dissenting from the Majority of the Chamberlain Commission had pointed out that the token rupee currency drove gold out of circulation and suggested that in order to induce the people to use their stored up gold, an assurance that they would be paid back in gold was necessary—a view which was repeated by Mr. (now Sir) Dadiba Dalal in his Dissenting Minute (para 61) to the Babington Smith Committee's Report.

Exchange Standard; and (iii) a Gold Standard proper, with or without a gold currency.

(i) *Sterling Exchange Standard* :—The working of the existing system was capable of being rendered more satisfactory by the amalgamation of the Gold Standard Reserve and Paper Currency Reserve so as to reconstitute on a statutory basis a single currency reserve, under the control of one currency authority, and by imposing a statutory obligation upon the currency authority to sell rupees for sterling (at the upper gold point) and to sell sterling for rupees (at the lower gold point) at a fixed parity. The Commission, however, objected that even such an improved system, would not be free from the threat implied in the rise in the price of silver and the dislocation caused in exchange and internal prices by a heavy depreciation of sterling. Though this was a remote danger, they thought that there was undoubted disadvantage for India in linking her currency to the currency of one single country (England). They thus conclude that “ were the standard of India to be an exchange standard, it should undoubtedly be a gold exchange standard, and not a sterling exchange standard. ” (para 25).

(ii) *The Gold Exchange Standard* :—The Commission admitted that a gold exchange standard could be secured by providing that the currency authority, instead of undertaking to buy and sell sterling, should undertake an obligation to buy and sell, at the upper and lower gold points respectively and to unlimited amounts, the currencies of any of the principal foreign countries with a gold standard (para 26) and that the Gold Exchange Standard ensuring the convertibility of the internal into international currency at the will of the holders, and with the improvements suggested above in relation to the Sterling Exchange Standard, would be superior to the latter, and would be no more subject to manipulation than the systems of the U. S. A. and Great Britain (para 28).

One of the most serious defects of the Gold Exchange Standard, however, would be that it would remain at the mercy of the price of silver, any rise in which above the melting point of the rupee would involve its disappearance. To meet

the situation by the issue of lighter rupees, nickel rupees and small notes would be open to strong practical objections, especially when it is remembered that under any exchange standard, the note would be internally convertible into silver rupees only and not into gold.

Moreover, the system would lack in simplicity which was premised as essential to secure public confidence. The mechanism of the exchange standard is too refined and the right of convertibility that supports the standard is too abstract and one of no direct concern to the general public for the present conditions in India. The backing which it supplies for the token currency is too intangible and invisible. Furthermore, the Commission hold that the suspicion in the public mind regarding the possibility of manipulation of the mechanism of an exchange standard to the detriment of Indian interests would be a fatal obstacle to the smooth working of that system. "In the present state of its development Indian public opinion will have confidence in one thing only as solid enough for a backing for its currency, and that is gold. It requires some link that is real, and not only real but conspicuously visible, between the currency of the country and gold.....Since a gold exchange standard cannot provide an efficient remedy for the defects of the existing system of Indian currency, to remedy these defects and to fortify popular confidence in the currency it is necessary to establish on a sure basis not only the external, but also the internal, convertibility of the token currency of the country into metallic gold." Thus the establishment of a true Gold Standard ought to be the goal of Indian currency policy (paras 31-32).

GOLD STANDARD FOR INDIA.

§ 3. Finance Department's Scheme :—The Commission, however, held that a gold standard does not necessarily imply a gold currency. They examined and rejected the principal proposal made by Sir Basil Blackett and other officials of the Finance Department of the Government of India.* Under this scheme it was proposed that the silver rupee should cease to be legal tender

* Vide appendices 5 to 7.

except for small amounts, say Rs. 50, after a period of ten years, during which time it would be convertible into gold currency. The scheme assumed that about Rs. 10 crores might be presented by the public for conversion into gold. In order to work the plan it would be necessary to take steps to attract to India a large additional amount of gold for currency purposes and for the conversion of the hoards. It was also contemplated to sell an amount of redundant silver equal to about thrice the world's production for a year. The ideal ultimately to be reached was the system in force in Great Britain under which the note is the sole full legal tender in circulation, and the gold value of the sterling is stabilised by the statutory obligation imposed upon the Bank of England to buy and sell gold at rates corresponding roughly to the par of exchange. We would have to wait a long time, however, before conditions in India are so far changed that a full legal tender metallic currency will no longer be necessary. In the meanwhile, the attainment of such an ideal system would be expedited by expanding the circulation of notes by making them convertible into full-valued gold coins and not merely into over-valued silver rupees. In this way the hoarding habits of the people will be discouraged by assuring them that when they make investments or deposits with banks of a certain gold value they will get back the same in gold value. The cost of the scheme was estimated at about Rs. $1\frac{2}{3}$ crores per annum during the first five years and thereafter from $\frac{2}{3}$ rds of a crore to 1:12 crores. The proposed limitation of the legal tender quality of the rupee was intended to relieve the currency system from any possible rise in the price of silver and to enable the constitution of the reserves to be simplified.

§ 4. The Commission reject the Scheme:—The commission rejected the scheme on the following grounds:—

(i) The effects of the Indian demand for gold of about £103 millions (exclusive of the normal absorption for arts, hoards etc.) on the world's currency, credit, and on gold prices and rates of interest would be adverse and were bound to produce their repercussions on India as a unit of the world's trade system. The

Commission invited attention to the views of Prof. Gustav Cassel that there was urgent need for economy in the use of gold as a commodity and money, as there was reason to fear that the supply of the yellow metal was likely to be found dangerously inadequate, and that general depression and fall of prices were to be expected, unless the nations took concerted action and practised the most rigid economy in the use of gold. The reconstruction of the currency and credit systems of European and other countries dislocated by the War would be greatly impeded by India's absorption of a large quantity of gold. There was a tendency to place a reliance on the ability of the United States to release the gold required in India, but the gold supplies held by the United States were exaggerated and did not exceed its own requirements for internal absorption and for helping forward the monetary reconstruction of other countries.

(ii) There was a large element of uncertainty in the estimates of the amount of gold required for giving effect to the scheme and it was impossible to be sure that the additional demand for gold could be spread over 10 years. There was also the possibility of people showing a markedly inconvenient preference for gold coins as against notes, and of the increased use of gold for hoarding and non-monetary purposes caused by the depreciation of silver. The scheme contemplated the reduction of the proportion of gold and sterling securities in the Reserve to gross note circulation to 30 per cent. But this was too low for safety, especially during the transition period. The external convertibility of the local currency would be seriously jeopardised if the transition to the new system coincided with an unusually bad year for Indian exports. Also, as soon as it became known that the status of the rupee was threatened, there was the possibility of the whole of the surplus stock of rupees being offered for conversion into gold. The Commission could not agree that the putting of gold into circulation was necessary to call forth the gold hoards, as was assumed in the scheme. The real remedy was development of banking and investment habits.

(iii) The effect of the scheme on the silver market of the world must also be considered. The future of the white metal

was very uncertain. There did not seem to be any large possibility of curtailed output from the mines even if the price of silver fell, since silver is largely won as a by-product. The prospect of demand for subsidiary currency in European and other countries is also gloomy, as notes, nickel and inferior metals are being used increasingly for this purpose. If therefore the Indian demand were to cease by the proposed dethronement of the rupee and her normal demand for silver were to be met by melting rupees, it is doubtful whether she would be able to realise a price of more than 24 d. per oz. for her surplus silver. Moreover, the gold price of silver was likely to be further depressed by the independent appreciation of gold owing to its shortage in relation to the demand for it.

(iv) The adoption of the scheme would lead to a heavy depreciation of the silver hoards. This would especially affect the poorer people who put their savings into silver ornaments, and who would find their stores of value depreciated by perhaps 50 per cent by the action of Government. If in other countries also the prospect of a fall in the price of silver led to its replacement by gold as a store of value, the depreciation of silver would be still heavier. The attempt to protect the value of Indian holdings of silver by the levy of an import duty on silver to disconnect its price in the world market from that in India, would probably not succeed, even if other objections to such a plan were to be waived.

(v) The Commission examine separately the effect on India of the probable reaction of these proposals on other silver-using countries, especially China. China is the only great silver standard country at the present time and perhaps the only great undeveloped market left for the expansion of international trade. She has long entertained the intention of introducing some form of gold standard, and the fulfilment of this intention was likely to be accelerated by India's announcement that she proposed to sell her surplus silver. This would induce a further fall in its price and bring about an appreciation of gold. The dislocation of the Chinese exchange caused by India's proposal to sell her silver would exercise a detrimental effect on the growing trade

of the world with that country, from which India could not possibly escape.

(vi) There was little possibility of India receiving the indispensable assistance of England and the United States in raising the credits that would be required for carrying the scheme successfully through. Both the countries viewed the scheme with alarm on the ground that it would retard the progress of monetary reconstruction in Europe, upset world prices, and would be fundamentally harmful both to India and to the rest of the world. Moreover, the United States would be unwilling to lend its support to the Indian scheme of a gold standard as it would deal a heavy blow to its great and traditional silver interest. In the absence, therefore, of a definite assurance regarding the amount of the gold required to carry out the scheme, it would be inexpedient for the Government to embark upon it.

The Commission also emphasise the heavy cost India would have to incur immediately in carrying out the scheme and the further indefinite cost resulting from the promotion of gold circulation and the consequent check to the natural growth of the note issue.

The Commission, therefore, reject the scheme as unacceptable, both on account of its unsettling effect upon monetary reconstruction and stabilisation in other countries and its injurious reactions on India, and they proceed to unfold their scheme of what they call *The Gold Bullion Standard*.

§ 5. The Gold Bullion Standard:—They argue that it is possible to have a true gold standard under which the currency is based on gold both in reality and in a manner that is conspicuously visible, without putting gold into circulation. “The essence of the proposal.....is that the ordinary medium of circulation in India should remain, as at present, the currency note and the silver rupee, and that the stability of the currency in terms of gold should be secured by making the currency directly convertible into gold for all purposes, but that gold should not circulate as money. It *must* not circulate at first and *need* not circulate ever.” (para 54),

The chief reason, according to the Commission, against putting gold into circulation is that, the larger the amount of such gold in circulation, the smaller the gold reserves and the greater the inelasticity of the credit structure based on them. They endorse the view of the Chamberlain Commission that, gold in circulation is of uncertain value for the support of exchange. They claim that the adoption of their scheme would ensure sufficient public confidence in the stability of the system—a special advantage ordinarily claimed for a gold currency—without sacrificing elasticity, and that it would carry India far along the road towards the ideal currency of the future, viz., a token currency of notes inconvertible for internal purposes. Another point in favour of the proposed scheme of the Gold Bullion Standard is that it promises to set up almost immediately a full gold standard and dispenses with any period of transition provided for in other schemes such as that of the Finance Department discussed above. While providing for the gradual strengthening of the gold reserves at a rate which will not have any unsettling effects on the existing world conditions, the scheme is capable of adjusting itself to any decision in future in favour of a gold currency, which it is impossible to introduce all at once. The Commission's own view is that it would be unwise to contemplate the introduction of a gold currency under any conditions, and therefore, while leaving the door open for the introduction of a gold currency, if the people of India desired it, they express the hope that India would, in course of time, come to look upon it as an obsolete and outworn ideal. The War has demonstrated to the European nations that they can do without a gold currency whose very utility is now being doubted. The restoration of the Gold Standard in England in 1925, has been effected without the re-introduction of gold into circulation and she has, therefore, practically adopted the Gold Bullion Standard to be worked through the agency of the Bank of England. In the U. S. A. also, gold which circulates in theory, does not circulate in practice. Indeed, some high authorities have expressed the view that gold in circulation is coming to be regarded as a sign of a backward civilisation.

The Commission invite particular attention to their proposal to impose an obligation on the currency authority to convert the local currency, not merely into foreign exchange as hitherto, but into metallic gold, and the obligation is absolute and unlimited and not conditional and circumscribed as formerly. India's gold resources in her existing reserves, the Commission believes, are adequate for this purpose. The obligation to be imposed by statute on the currency authority will be to buy and sell gold without limit at rates determined with reference to a fixed gold parity of the rupee but in quantities of not less than 400 fine ounces, no limitation being imposed as to the purpose for which the gold is required. This is calculated to ensure the stability of the gold value of the rupee and the stability of exchange within the gold points corresponding to the selected parity. Gold is thus made the real standard of value. The rupee is linked to gold and not to sterling or any other currency or group of currencies. While the system is an absolute gold standard and not an exchange standard as hitherto, because rupees and notes are to be convertible into gold bars for *any* purpose, the compensatory mechanism of the exchanges is preserved, as gold bars are not currency. The currency is expanded when notes or rupees are issued by the currency authority in exchange for gold bars, and it is contracted when it gives gold bars for notes and rupees, and thus the stability of the gold value of the currency at the selected parity is preserved.

The Commission claim that their scheme of a gold bullion standard not only ensures stability, but also simplicity and certainty, as the statutory right of convertibility of currency into gold without limit of amount is intelligible even to the uninstructed and supplies a backing to the currency system that is tangible and visible. It establishes the principle that gold is the standard of Indian currency at a fixed ratio, and that the currency authority admits it, and must maintain it. In short, the scheme has all those characteristics necessary to inspire public confidence, and promote habits of banking and investment and discourage hoarding.

There is no reason to fear that the drain on the gold reserves for the conversion of rupees will be sudden, as (i) the legal tender quality of the rupee is to be left intact; (ii) the currency authority will so fix the rates for the sale of gold as not to compete with the bullion market (see § 6), and the holders of rupee hoards can convert them into gold by buying it in the open market as at present.

The Commission observe that the existence of a large volume of currency in hoards is a great obstacle to efficient control by the currency authority over currency, credit and the money-market through expansion and contraction of currency. The conversion of rupees into gold bars and not coin, the demonetisation of the sovereign, (which is proposed in order that the existing hoards in the shape of gold coins may be prevented from entering into circulation, and the system of gold saving certificates explained below in § 7), will all tend to rob the hoards of their power of disturbing internal prices and money rates.

§ 6. Buying and selling rates for gold :—The Commission suggest certain modifications of the principle that a sound gold standard postulates a statutory obligation upon the currency authority to buy and sell gold at a price equivalent to the par value of the monetary unit, in view of the unusually large non-monetary demand for gold in India for social purposes. Rates fixed with reference only to the par value of the rupee and without reference to the costs of importation and to any deviation in the value of the currency from its gold parity would make the currency authority the cheapest market for gold. This would not only destroy the gold bullion market in India, but would also saddle the currency authority with the work of selling gold for non-monetary uses, which does not properly belong to it. In order to free it from this obligation, the Commission suggest that the selling prices of gold should be fixed at such rates as will make possible the replenishment of the stock of gold without loss by importation from London.*

* The par value of the rupee as proposed by the Commission is 1s. 6d. (8.47 grains of fine gold) or Rs. 13.37 for £1. The par value of a tola of gold at this rate is Rs. 21 as. 3 pies 10.

The Commission propose that the legal tender quality of the sovereign should be removed so long as the amount of gold in the reserves is not big enough for the introduction of a gold currency, and so long as no definite decision in favour of a gold currency is taken. Otherwise, the gold from the reserves might in certain circumstances pass into circulation without effecting any contraction in the currency and thus without securing the compensatory effect of the exchanges. The demonetisation of the sovereign (and the half-sovereign) would not involve any hardship as they have long ceased to function as currency owing to the continued retention of the 2s. rate on the statute book since 1920, and the consequent undervaluation of gold as currency. In case they are held as a store of value, there would be no loss to their holders, the coins being fully valued, even if they cease to be legal tender. Since a real gold standard with a gold currency was unattainable at least immediately, the Commission argue that there need not be any hesitation in sacrificing the shadow of an unnecessary and little used gold coin of legal tender, in order to obtain the substance of a real gold standard.

§ 7. Introduction of Savings Certificates payable in gold.—The Commission realise that as the obligation of the currency authority to buy and sell gold related to quantities of not less than 400 ounces of gold, it would be the bankers and bullion brokers who will make direct use of the provision and not the people at large. To secure popular confidence in the currency system, therefore, the Commission proposed that Government should offer for sale savings certificates redeemable in three or five years in legal tender money or gold at the option of the holder, and giving him an attractive yield in interest. This would of course involve the strengthening of the gold in the currency reserves. The Commission claimed several advantages for these certificates. They would stimulate investment and call forth hoards and demonstrate to the holder the solidity of the gold basis of the rupee. The certificates would supply a direct and visible proof that gold is the standard of value, and that the rupee and gold are mutually convertible one into the other. The chief benefit that is claimed for a gold currency would thus be achieved

without any of the risk, expense and inconvenience involved in putting gold into circulation.

§ 8. Convertibility of Notes into silver rupees:—The Commission recommended strongly that the existing anomaly in the Indian currency system due to the obligation of the Government to convert one form of note, viz., the note printed on paper into another form, viz., the rupee, which is merely a note printed on silver, must be removed sooner or later to rid the system of the threat involved in a rise in the price of silver. Moreover, the silver branch of the Paper Currency Reserve was of little value for external convertibility. This reform would be effected in connection with the proposed scheme of the Gold Bullion Standard, under which the notes would be converted into gold, which would provide a more solid backing than that of the silver rupees. Of course the promise of converting the existing notes into rupees must be kept. But no obligation for conversion into silver rupees should attach to the new notes. It is however essential that facilities for the free exchange of notes for rupees should be provided, so long as the people desire to obtain metallic rupees, in order to inspire public confidence and ensure the popularity of the note issue. No fresh rupees should be coined for a long time to come, but this need not cause any inconvenience as the existing stock of silver bullion and rupees (about 85 to 90 crores), which might be expected to be strengthened in due course by the coming out of the rupee hoards, would be quite ample for this purpose. In this manner the change in the legal status of the notes will be quite unfelt.

The Commission propose the re-issue of the one-rupee notes with full legal tender power and like the other notes of the new status, not legally convertible into silver rupees. While such a step may retard the absorption of the surplus silver rupees now in the Reserve, it will have the counterbalancing advantage of helping to popularise the use of notes and offering a way out, in case the price of silver should ever again rise above the rupee-melting point.

The withdrawal of the existing legal right of convertibility

of notes into rupees makes it necessary to impose a statutory obligation on the currency authority to convert all notes, excepting the one-rupee notes, on demand into legal tender money, i.e. into notes of smaller denominations or silver rupees *at the option of the currency authority*, though all reasonable demands of the public for metallic currency should be met in practice.

The Commission are opposed to any alteration in the legal tender quality of the rupee, and believe that their other proposals overcome the reasons urged in favour of a such a course.

§ 9. Unification of the Paper Currency and Gold Standard Reserves :—The Commission recommended that the Paper Currency and Gold Standard Reserves should be combined into one Currency Reserve so as to ensure the efficiency of its working and make it simpler and more intelligible to the public. The existing practice leads inevitably to a certain amount of overlapping between the two reserves, for while the Paper Currency Reserve has to be used to support exchange, the Gold Standard Reserve has to be drawn upon for the external convertibility of the note. The proposed amalgamation will be facilitated by the removal of the legal right of convertibility of the note into silver rupees.

§ 10. Composition of the New Reserve:—The main recommendations with regard to the composition of the Reserve are as follows :—(i) The composition and proportion of the Reserve should be laid down by statute so as to ensure automatic expansion and contraction of currency and the compensatory effect of the exchanges; (ii) The proportional reserve system should be adopted, and gold and gold securities should form not less than 40 per cent of the Reserve. The currency authority should strive to work up to a reserve ratio of 50 to 60 per cent. The gold holding should be raised to 20 per cent of the Reserve as soon as possible and to 25 per cent within 10 years. During this period no favourable opportunity of fortifying the gold holding should be allowed to escape unutilized. Of the gold holding at least one-half should be held in India. (iii) The silver holding in the reserve should be very substantially reduced during a transitional period of 10 years. (iv) The balance of the reserve should be held in self-liquidating trade bills and Government of India

securities. The "created securities" should be replaced, by marketable securities within ten years. (v) Rs. 50 crores may be regarded as the approximate liability in respect of the contractibility of the rupee circulation. An amount equal to one-fifth of the face value of any increase or decrease in the number of silver rupees in issue should be added to or subtracted from this liability, and the balance of profit or loss should accrue to or be borne by the Government revenues.

The Commission insist that the fortification of the gold reserves in the manner described above is necessary (i) to enable the currency authority to discharge its obligation to sell gold in exchange for currency and in view of the new status of the notes which are convertible into gold; (ii) to enable the Government to encash the Gold certificates in case they prove to be popular; and (iii) to facilitate the introduction of a gold currency if it is decided to have it. The Commission claim that this gradual strengthening of the gold reserves will involve the minimum of risk and expense.

The Commission recognise that silver reserves are out of place in a gold standard system, but the peculiar position of the rupee, due to the fact that it forms a large proportion of the total circulation and the considerable seasonal ebb-and-flow in this form of currency make it necessary to hold a part of the reserve in silver. The one-rupee note may be expected to reduce the quantity of rupees required and the recommendation is therefore made that the silver holding in the reserve should be lessened in the period of transition, from Rs. 85 crores (the figure at which it stood on 30th April 1926) to Rs. 25 crores.

The Commission recommend that the rupee securities of the Government of India held in the reserves should be limited to an amount equal to so much of the circulation as is unlikely to be withdrawn plus such further amount as can be easily realised without disturbing Government's credit. This limitation is thought to be necessary because such securities are less desirable as assets than trade bills, which, unlike the former, possess the quality of automatically expanding and contracting currency in accordance with the needs of the country, independently of the

The following illustration makes the idea quite clear.* Suppose that as compared with 1913, which is taken as the base year, prices in the United Kingdom have risen to an index of 150 and that French prices have risen to an index of 300. If the pre-war rate of exchange were 25 francs to the £, the new normal will be 50 francs to the £. Thus:-

$$\begin{array}{rclcl}
 300 \text{ present francs} & = & 100 & \text{pre-war francs.} \\
 & = & 4 & \text{pre-war pounds.} \\
 & = & 6 & \text{present pounds.} \\
 \therefore 50 & \text{,,} & = & 1 & \text{present pound.}
 \end{array}$$

If the actual exchange rate differs from the purchasing power parity thus arrived at, then we are justified in inferring that equilibrium is not established and that, in the course of time, forces will come into play to bring the actual exchange rate and the purchasing power parity closer together.

Suppose in the above example, the actual exchange between the franc and sterling does not coincide with the calculated parity and that the pound instead of being quoted at 50 francs, is quoted at 55 francs. In that case, French products will be cheap to British purchasers and British goods will be dear to French purchasers. A British merchant by spending £100 could obtain 5500 francs, and with that sum in francs he could buy French goods, which when sold in England, could bring £110. Conversely a French merchant could only get £100 for 5500 francs, and for that sum would merely be able to purchase British goods to the value of 5000 francs in France. British imports from France would thus receive a stimulus and British exports would be checked. The increased demand for francs arising in this manner will raise the price of the French currency until the exchange settles at about 50 francs.

§ 14. Limitations of the Doctrine:—The Commission recognised various practical difficulties in applying the doctrine for solving the problem which they set themselves. In the first place, they said, it would be difficult, if not impossible, to pursue

* The illustration has been borrowed from D. T. Jack: *The Restoration of European Currencies*, pp. 15-16.

any argument on the subject of the movement of price levels, without making use of index figures in some form, and index figures were not an infallible guide and might easily lead one astray. Special caution is necessary in using them for the purpose of comparing the range of price levels in two or more countries over a particular period, because the figures are necessarily compiled in different ways in different countries. Moreover, the basic year selected may not be equally suitable in all the cases concerned. For example, there may have been some local peculiarity in the circumstances of the basic year, or the character of the production may have changed during the period in one or more of the countries. As regards the statistical employment of the doctrine of purchasing power parity, they remark that, quite apart from the imperfections of the Indian figures of prices, the employment of index numbers implies the important assumption that changes in the prices of goods entering international trade have been followed by similar changes in the prices of all other goods. As J. M. Keynes has put it, "The theory does not provide a simple or ready-made measure of the 'true' value of the exchanges. When it is restricted to foreign-trade goods, it is little better than a truism. When it is not so restricted, the conception of purchasing power parity becomes much more interesting, but it is no longer an accurate forecaster of the course of the foreign exchanges."* The Commission, therefore, admit that the theory can supply only a very approximate guidance, and that its practical utility is of a strictly limited character.

§ 15. Conclusions regarding price-adjustment:—Bearing these limitations in mind, they proceed to examine the available statistical data and summarise their conclusions as follows:—

From December 1922, to June 1924, the gold exchange value of the rupee remained fairly stable round 1 s. 3 d. gold. During the same period the rupee price level remained fairly steady round 176. From July 1924, to January 1925, the rupee rose sharply to the neighbourhood of 1 s. 6 d. gold, and since the end of May 1925, it was held within 1 s. 6 d. gold points. From July 1924,

* Keynes : *Monetary Reform*, p. 94.

to June 1925, the rupee price level fell from 179 to 157 and had varied since then between the limits of 163 and 153. They thus observe that--

(i) during 18 months, while the rupee was worth about 1 s. 3 d. gold, the rupee price level ranged round a mean of about 176.

(ii) In the succeeding year, while the rupee was rising to 1 s. 6 d. gold, the rupee price level fell below 160.

(iii) Since then, while the rupee had remained, or been held, at about 1 s. 6 d. gold, the rupee price level had ranged round a mean of about 158, and had begun to show a tendency to fall in sympathy with world prices.

The level of world gold prices had been approximately the same at the beginning of period (i) and at the end of period (iii). They, therefore, thought that during the period of change, there was a mutual adjustment of prices and exchange, and that a substantial equilibrium had been attained about the middle of 1925 and had since been maintained.

This analysis appeared to the Commission to provide a conclusive answer to the main contention of those who doubted the fact of substantial adjustment of price to the 1 s. 6 d. ratio. Their contention was that, it was not till June 1925 that the rupee had attained 1 s. 6 d. gold. Since then the rupee prices had been practically stable in relation to the world prices. Therefore adjustment had still to take place. The Commission's answer to this was that although the rupee did not definitely reach 1 s. 6 d. gold till June 1925, it had between July 1924 and January 1925 already traversed more than 80 per cent of its upward journey from 1 s. 3 d. to 1 s. 6 d. gold; and that before June 1925 there had already taken place a heavy fall in rupee prices in relation to world prices, which the Commission was inclined to regard as the complement of the steep rise in exchange.

As a further indication of equilibrium between external and internal prices, the Commission point to the steadiness of the exchange during the 12 months preceding. They argue that exchange is the mechanism by which differences in these two price levels are adjusted. So that when exchange remains steady

over a fairly long period, the inference was permissible that there were no differences to be adjusted. They also hold that the so called manipulation by Government in order to keep the exchange at the level of 1 s. 6 d. merely amounted to a normal addition of currency during the busy season and equally normal contraction at the end of it.

That there was no disequilibrium between internal and external prices was also indicated by the fact that neither exports nor imports were adversely affected as would have been the case if the rupee had been either under-valued or over-valued internally in comparison with its external value.

§ 16. Wages:—The Commission also came to the conclusion that there was a general adjustment of wages with prices and exchange. They argue that when exchange and prices have been steady over a considerable period, there is justification in assuming that wages are in adjustment unless there are clear indications to the contrary. The statistics of foreign trade appeared to the Commission not only not to yield any such contrary indication but rather to strengthen the assumption. The depression in agriculture which is pre-eminently India's greatest industry, was in no way due to lack of adjustment between agricultural wages and the exchange. Similarly with regard to the Government services, the Commission observe, that the increase in the value of the rupee to 1 s. 6 d. had enabled Government to refuse increases of pay which it might otherwise have been difficult to resist. In the manufacturing industries also, the Commission were unable to discover any general maladjustment. In the Jute mill industry of Bengal they found that the wages were in line with existing price levels and cost of living. As to the steel industry it was suffering not so much from high wages as from the stress of foreign competition, stimulated in some countries, e. g. Belgium, by depreciating exchanges and if relief was necessary, the way to grant it was not by manipulation of the currency. If foreign countries allowed their currencies to depreciate continuously, India could not possibly think of entering on a course of competitive inflation in order to keep pace with them. In the Cotton mill industry wages were apparently still

too high, for whereas the index figure of wages of mill-hands was 231 (as compared with 100 in 1914), the index numbers of wholesale prices, retail food prices, and cost of living were only 150, 150, and 153 respectively. This indicated that either the pre-War rate of wages was too low or the existing rate was excessive. However that might be, the Commission thought it highly undesirable to produce a concealed reduction in wages by adopting the lower ratio, and they further held that in any case it was highly improbable that the desired equilibrium could be secured in this manner.

§ 17. Effect on contracts:—The Commission next proceed to consider the effect of the 1 s. 6 d. rate on the outstanding contracts. They admit in this connection that many of the current land revenue settlements had been made when exchange was at 1 s. 4 d., but in view of the great rise in prices since 1914, the real incidence of land revenue, measured in terms of commodities, had been very materially lightened, and, therefore, the 1 s. 6 d. rate could not be regarded as constituting any great hardship.

With regard to other long-term contracts, the Indian exchange had been more or less unstable during the previous 8 or 9 years when it was never at or near 1 s. 4 d. for any length of time so as to admit of adjustment on the basis of the old rate, and the Commission contended that contracts and arrangements concluded prior to 1918, and still in existence did not bulk as largely in the economic life of the country as those concluded during the subsequent 8½ years, during which period the exchange had been in a state of flux.

In any case, after the prolonged disturbances which had taken place, it was impossible to do absolute justice to the long-term creditor and debtor by fixing on any particular rate of exchange. The Commission thus concluded that from the point of view of contracts as from that of prices and wages, the least disturbance would be caused and the least injury would be done to all the interests concerned, by adhering to the *de facto* rate.

§ 18. Arguments for 1 s. 4 d. considered:—The Commission

then consider some of the more important arguments for the lower ratio only however, to reject them one by one.

As regards the contention that the 1 s 4 d. rate is the "natural" rate for the rupee, the Commission argue that the only rate which could be properly regarded as natural is the figure at which prices were in adjustment with the existing volume of currency and in equilibrium with external prices. And from this point of view 1 s. 6 d. appeared to be clearly the "natural" rate under the existing circumstances. If, on the other hand, by natural rate was meant that rate which would establish itself in the absence of statutory enactment or executive action to anchor the rupee at a particular point, on this sub-position there would be such extensive fluctuations in the rate of exchange in a country like India with its wide seasonable fluctuations of trade, that it would be impossible to distinguish any particular rate as "natural."

With regard to the criticism of the action of Government in intervening in April, 1926, to prevent a fall of exchange below 1 s. 5 $\frac{3}{4}$ d., the Commission point out that no exception had been taken to the earlier action of Government, in October, 1925, in intervening to prevent a rise in exchange above 1 s. 6 $\frac{3}{8}$ d. And they hold that if either of the tendencies was to be regarded as natural, i. e., the genuine reflection of trade conditions, it was the earlier tendency to rise above the 1 s. 6 d. upper gold point. This was evidenced by the fact that the rate was only kept down by large purchases of sterling and the accompanying expansion of currency, whereas the later falling tendency was due not to any genuine trade factors but largely to speculation on the possibility of a lower rate than 1 s. 6 d. being recommended by the Commission, and very little effort was actually required to arrest that tendency.

The argument that the 1 s. 6 d. rate had come into being through Government manipulation, even if it had been based on facts, was irrelevant. For in choosing the rate for the final stabilisation of the rupee the facts of the present had to be faced to whatever causes they may have been due. When prices and other conditions were in adjustment with those in the world at large on the basis of an existent exchange rate, the question of

the means by which that rate had come into existence had no bearing on the extent or violence of the economic disturbances to be expected from an alteration in the rate.

The Commission point out that, broadly speaking, all the arguments in favour of reversion to 1 s. 4 d. merely showed that during a period of adjustment of conditions to that rate, certain sections of the community (e. g., debtors, exporters, and employers of labour) would benefit at the expense of certain other sections (e. g. creditors, importers, and wage-earners); they did not show that there would be any substantial permanent benefit even to any section at the expense of another, still less to the country as a whole.

The economic effects of a reversion to 1 s. 4 d. were, in the judgment, of the Commission, likely to be profoundly disturbing. For even if the view that prices and wages had been substantially adjusted to the 1 s. 6 d. rate were challenged, it could not be seriously contended that they were in any way adjusted to the rate of 1 s. 4 d., because, as already pointed out, that rate had never been in stable operation sufficiently long during the preceding eight years or so. In so far as adjustment had taken place at all, it must have been to the higher rate of 1 s. 6 d. The reversion to 1 s. 4 d. under these circumstances was bound to produce a general rise of prices to the extent of $12\frac{1}{2}$ per cent, a change which would press severely on consumers in general and especially on the poorer paid members of the literate classes. It would also result in an arbitrary reduction of the real wages of labour for which there was no justification in equity or in expediency. The finances of Government, central as well as provincial, would be seriously upset by a reversion to 1 s. 4 d., which would further postpone indefinitely the long and loudly called-for abolition of Provincial Contributions. The only right course under the circumstances, therefore, was to stick to the *de facto* ratio.

§ 19. Minute of Dissent:—Sir Purshotamdas wrote a Minute of Dissent in which he differs fundamentally from his colleagues particularly on the question of the ratio and is emphatically opposed to stabilisation of the rupee at the *de facto* rate of 1 s.

6 d. In a lengthy historical retrospect of the Indian Currency and Exchange system he points out how the Government had made up their mind to raise the exchange to 1 s. 6 d. and had surprised the Commission with a *fait accompli* so as to prejudice both their inquiry and finding. He shows how the Government threw away the opportunity in September and October 1924 of stabilising the rupee at the pre-war rate of 1 s. 4 d. and restoring the long-established standard of money payments and describes the steps which the authorities took to screw up the exchange to 1 s. 6 d. All the while the fictitious ratio of 2 s. gold on the statute book was utilized by Government as a potent weapon for rigging up the exchange and this official administration of currency involved its serious contraction.

Sir Purshotamdas regarded the proposal to fix the exchange at 1 s. 6 d. with grave apprehension as likely to cause a disturbance in the economic organisation of the country, the magnitude of which, he said, was difficult to estimate, and the consequences of which would not only hamper economic development but might even prove positively disastrous. His main conclusions regarding the ratio controversy were as follows:—(i) The greater part of the general adjustment of prices was still to come. (ii) No adjustment in wages had taken place and none was likely without a struggle. (iii) Until adjustment was complete, the 1 s. 6 d. ratio presents the foreign manufacturer with an effective though indirect bounty of $12\frac{1}{2}$ per cent, which “would place a heavy strain on Indian industries, nascent and established and protected industries would consequently need a further $12\frac{1}{2}$ per cent. countervailing protection or assistance by subsidies. (iv) A change in the ratio hit the large bulk of the debtor class drawn from the ranks of the agriculturists whose total indebtedness has been estimated at Rs. 600 crores for British India only. Being an old debt of long standing, it was natural to assume that it was mostly contracted on a 1 s. 4 d basis. Thus a change to 1 s. 6 d. would mean an additional burden of $12\frac{1}{2}$ per cent on the debtor class. Under the head of contracts, therefore, the higher figure of 1 s. 6 d. had little to recommend it, and very much against it. (v) The adverse effect on public finances of a reversion to 1-4 had been exaggerated. As against the increased

rupee expenditure in regard to sterling liabilities in England, there would be an increased customs revenue of 2.62 crores under 1-4., increased receipts from income tax owing to industries being spared the disturbance inseparable from 1-6, and the avoidance of bounties etc. to industries as cover against foreign competition. Moreover, whatever the advantage to the Government, it must be remembered that it is not obtained without being paid for by the producer who has to accept so much less in rupees for his produce. (vi) The alleged adverse effects of a reversion to 1s. 4d. had been exaggerated. A rise in the rupee prices of exports is not a direct hardship to any one in India. As to imports becoming dearer this may to some extent affect the foreign manufacturer, but he may expect to be compensated by the better purchasing power of India as a whole. Regarding prices of articles locally produced and consumed, as prices had not yet adjusted themselves to 1 s. 6 d., the fear of a rise of $12\frac{1}{2}$ per cent was groundless. (vii) The adverse effects of 1 s. 4 d. on a small section (about 21 per cent) of the population consisting of the more poorly paid members of the literate classes must be allowed less weight than the suffering which the higher ratio entailed in the case of the remaining 79 per cent of the total population. As to labour, the existing rate of wages was sufficiently high to cover a possible rise in prices caused by the adoption of 1 s. 4 d. In any case there is the compensating advantage of a continuity of employment due to the fact that the lower ratio would ensure greater prosperity to industry and agriculture, while the higher ratio was sure to injure both. (viii) The sanctity of the standard of money payments once established must be respected. Any tampering with it was bound to have serious political effects in India causing distrust in the currency and financial systems of the country. The pre-war ratio of 1 s. 4 d. was disturbed as a result of the War in common with the ratios of other countries of the world. But other countries had invariably striven to restore their pre-war ratios. At its worst the question in India was one of balancing the disturbance which might be caused by a reversion to 1s. 4d. on the one hand, and the adoption of 1s. 6d. on the other. Even if it were granted that the disturbance

involved in either case was equal, the decision should still be in favour of 1 s. 4 d.

§ 19. The Ratio controversy examined:—The Majority Report and the Dissenting Minute together provided a complete armoury from which combatants on either side drew their weapons in the fierce controversy which raged round the question of the ratio. Both the sides appear at first sight to be so equally balanced that it is difficult for the unprejudiced observer to make up his mind as to which is really the stronger of the two. Weighing the arguments on either side, both seem to feel equally heavy, and sounding them, both seem to become the mouth equally well. On a closer scrutiny, however, it is possible to detect several flaws in the reasoning employed by the advocates as well as the opponents of the new ratio.

The Majority begin by pointing out that the index numbers on which they base their arguments regarding the price adjustments to the 1 s. 6 d. ratio, are by no means an infallible guide. But by the time they finish their calculations based on these self-same imperfect index numbers, they somehow succeed in attaining to an absolute and well-nigh helpless conviction that substantial adjustment had undoubtedly taken place, and they work themselves up to an almost apostolic fervour in favour of 1 s. 6 d., forgetful of their own warning about the unreliability of the index numbers. Sir Purshotamdas also lays himself open to a similar criticism when from the same statistical material as employed by the Majority he obtains a precisely opposite conclusion and shows an equally unwarranted and unquestioning faith in the accuracy of his results.

Again, the arguments of the Majority that wage adjustments were practically complete do not appear very convincing. For example, no statistical evidence is adduced to show that agricultural wages were in adjustment. On the contrary, Sir Purshotamdas gives figures indicating that no decline in agricultural wages had occurred. * In the case of Government services, the Majority are driven to resort to the negative and unsatisfactory argument that the 1 s. 6 d. ratio

* See Minute of Dissent, Para 100.

had prevented an increase in the salaries of Government servants which would otherwise have been inevitable. It is only as regards the Jute industry that they are able to make a positive assertion that the wages were in correspondence with current prices and cost of living. But in the case of the important cotton industry they are compelled to admit a serious maladjustment between wages and prices.* Their observation that even if the wages were to be lowered by $12\frac{1}{2}$ per cent, this would not go very far in relieving the depression in the industry is irrelevant, as the question at issue was whether or not the wages had been adjusted to the 1s. 6d. rate. They appear similarly to shift their ground when they address themselves to the question whether the outstanding contracts would be affected by the rate of 1s. 6d. They do not content themselves with trying to show that the bulk of the contracts were short-term and therefore not affected by the new ratio. They go out of their way in attempting to prove that even in the case of the long-term contracts the 1 s. 6 d. rate did not constitute a hardship, because, e. g., in the case of the land revenue settlements the real incidence of land revenue had been materially lightened owing to the very great rise in prices since 1914. They argue against the concealed reduction of the wages of the mill-hands by manipulating the exchange, and, for the sake of consistency, they should have regarded the concealed increase in the land revenue assessment as one of the valid points against the 1. s. 6 d. ratio. The Commissioners thus fail to recognise the full force of the objections to the rate proposed by them from the point of view of long-term contracts.

They make much of the fact that, beginning from the year 1917, for about $8\frac{1}{2}$ years, the rate was at or about 1s. 4d. only for a short period. They argue from this that the great bulk of the contractual obligations were incurred under modern conditions and that, so far as these were concerned, it was reasonable to suppose that they originated, for the most part, when conditions were based on the 1 s. 6 d. rate, or at all events after exchange had broken away from 1s. 4d. †

* Report, para 193.

† Paras 195-96.

But although conditions were in a state of flux during the 8 or 9 years referred to by the Commission, it is not unlikely that a considerable number of contracts might have been entered into on the basis of 1s. 4d. For, it cannot be denied that this had come to be widely regarded as the permanent or natural ratio having been in uninterrupted operation for the long pre-war period between 1898 and 1914, and there was a general expectation that when the upheaval caused by the War had spent its force and conditions assumed their normal complexion, the pre-war ratio would again be restored. In para 198 of the Report, the Majority refer the falling tendency of the exchange in April, 1926, to the speculation on the possibility of a lower rate than 1s. 6d. being recommended by the Commission. This shows that if the Commission had actually advised a return to the 1s. 4d. ratio, this would have appeared to most people as the most natural thing in the world.

The Majority, while admitting that the influence of the ratio on Government finances must not be regarded as a decisive factor, were nevertheless not able to resist the temptation of exploiting the argument for all it was worth and more. We cannot help thinking that it would have been better if they had left this argument alone. It is not contended that the effect on public finances should under no circumstances be considered. We have in fact already admitted, in supporting Government action in demonetising silver in 1893, that the embarrassments and uncertainties besetting Government finance constituted a powerful argument for the closure of the mints to silver. But there was nothing to show in 1925 that the difficulties of Government would have been absolutely overwhelming under the ratio of 1 s. 4 d., and that drastic action of some kind would have been necessary on their part to meet these difficulties in default of the higher ratio. It has been suggested that when Government adopted the 2 s. gold ratio in 1920, they were primarily moved to do so by the financial reason. The impending constitutional changes and the separation of Imperial from Provincial finance which they involved meant that the Government of India could no longer levy contributions on the Provinces as freely as they had been wont to do. The high exchange there-

fore appeared to them a god-send enabling them to balance their budget without courting popular discontent by raising taxation.* We have already dwelt on the disastrous consequences of the action taken by the Government on the Babington Smith Committee's Report. In view of these past happenings the Commission should have desisted from even appearing to attach any great importance to considerations of public finance in deciding the currency policy, especially as these considerations were not of an absolutely compelling character.

As we have already seen, the Majority objected to a reversion to 1 s. 4 d. on the ground that it would entail undeserved suffering to the poorer paid literate classes. Considering that these classes had suffered more than any others by the recent rise in prices and that much of the burden arising from the extension of the new policy of protection which has been recently initiated is sure to fall on them, there is *prima facie* a good case for any step tending to promote the interests of the middle and the lower middle classes. But the general rise of prices to the extent of 12½ per cent feared by the Majority as certain to result from the reduction of the rate to 1s. 4d. assumed what really had not been proved, viz., that prices had already completely adjusted themselves to 1s. 6d. Further, even taking complete adjustment for granted, there were reasons for hoping that the full rise of 12½ per cent would not have actually manifested itself because it would probably have been counteracted a good deal by the tendency which was visible for the world prices to fall.

The strongest point made by the Majority was that the high rate had enjoyed an unbroken existence for over a year and that presumably a good deal of adjustment had taken place during this period. Most of their other arguments do not seem to stand the test of severe analysis.

It can equally well be shown that the champions of 1s. 4d. did not always use arguments which were entirely unexceptionable and economically sound. For example, they never wearied of harping on the excessive deflation of currency indulged in by Government in order to maintain the ratio at 1s.

* See Ambedkar, op. cit. pp. 207-208.

6d. But if the deflation was as great as it was made out to be, it must have substantially brought down the general level of prices. To admit a considerable fall of prices, however, was to admit a more or less complete adjustment to the higher ratio.

The opponents of the higher ratio dwelt on the increase in the burden of rural indebtedness caused by it, but they did not take into account certain compensating advantages accruing to the agriculturist from cheaper implements and, in general, a decreased cost of production. They also failed to take cognisance of the fact that a good deal of the agricultural debt is incurred in kind and not in money, and that part of it also consists of short-period obligations.*

By far the strongest argument in favour of the old ratio was that stabilisation at 1 s. 6 d. appeared like wanton tampering with the standard of value. Even if we choose the most favourable ground for the advocates of 1 s. 6 d. and assume that economic disturbance would have been greater under 1s. 4d., the evils proceeding from this disturbance would have been more readily acquiesced in by the people. As it is, the departure from the old ratio has vastly increased the number of currency malcontents and presented the critics of Government with a new grievance to which there is already a tendency of attributing every imaginable evil. For the next Budget session (1929), an enterprising member of the Legislative Assembly, Mr. Sesha Iyengar has given notice of a question on the exchange ratio inquiring "whether Government are aware that since April, 1927, the buying power of this country and net registration of Joint-Stock companies are going down and that unemployment among the middle and lower classes is getting more widespread and acute. If so, will Government be pleased to take immediate steps to restore the 16 d ratio, as there is a general feeling that the present state of things is directly traceable to the fixation of the 18 d. ratio early in April, 1927." All this appears to us very far-fetched but it confirms our view that the new ratio will be made answerable for every kind of misfortune and it bids fair to take its rank along with the drain theory as an all-sufficient explanation for every conceivable evil.

* See Coyajee, *India's Currency Exchange and Banking Problems*, p. 10.

No doubt the evils predicted by some people from the higher ratio were exaggerated and it would not be difficult to show that in certain directions progress has been maintained in spite of it, or at least that there has been no catastrophic disturbance. Sir J. C. Coyajee, for example, argues that "if the alleged great increase of the burden of debt and the material reduction of cultivators' income were positive facts, we should expect to see the following symptoms making their appearance without fail: (a) the growth of the capital and deposit of the rural societies would have been materially checked and even reduced; (b) the proportion of arrears to outstandings would increase largely; (c) the rate of interest would rise remarkably; and (d) loans for unproductive purposes, like repayment of debt, would increase materially." Similarly, "there would have been an immense number of suits and forfeiture proceedings by Mahajans and Sahukars all over the country, because no creditor can rest in peace while his claims are being submerged in such an avalanche of new liabilities; and by now immense areas of land should have passed into the hands of the Sahukars."* The author of these remarks goes on to point out that none of these disasters has come to pass. The latest Annual Report (1928) on the working of Co-operative Societies in the Bombay Presidency refers to the remarkable fact that there was an increase in the working capital by nearly a crore of rupees in spite of floods in Gujarat and certain parts of Sind. It is only fair to mention, however, that the Report also complains of the arrears having increased. All the same, the broad conclusion remains intact that no cataclysmic disaster has overtaken agriculture on account of the new ratio.

It would be more difficult to arrive at any such comforting conclusion with regard to manufacturing industry, especially certain branches of it like the Cotton Mill industry.¶ The

* See Coyajee, op. cit. p. 4 and pp. 7-8.

¶ Mr. J. M. Keynes arguing against the rise in the international value of sterling in England by means of deflation pointed out that the export industries were the first to suffer by such a procedure. "If everyone was accepting a similar reduction at the same time, the cost of living would fall, so that the lower money wage would represent nearly the same real

economic historian of the future will not record the period that has passed since the new ratio was made effective as among the most prosperous for business and industry in this country. It would be impossible to say how far the depression that has hung over them in recent years is due to the painful process of readjustment necessitated by the new ratio. The cotton mill-owners firmly believe that it is due to the ratio and as evidence of this they can point to the fact that wages have not yet adjusted themselves to it and the workers have successfully resisted so far the attempts of the millowners to lower them.

It is open for the opposite side to argue that industry and commerce would have been in an even worse plight, if the country had gone back to the old ratio. This, however, takes for granted something of which no one could be quite sure, viz, that more than 50p.c. of the transition to the 1 s. 6 d. had been accomplished. We have already suggested above that the evidence adduced in support of the Commission's view that the major part of the adjustment had already been over when they began their deliberations, is far from being convincing. We have gone further and argued that even if the reversion to 1 s. 4 d. had meant slightly greater disturbance—and this is the utmost that need be conceded by any one † impartially weighing all the evidence produced—it would have been worth while risking it for the sake of the old standard.

wage as before. But in fact, there is no machinery for effecting a simultaneous reduction. Deliberately to raise the value of sterling money in England means, therefore, engaging in a struggle with each separate group in turn, with no prospect that the final result will be fair, and no guarantee that the stronger groups will not gain at the expense of the weaker." See Keynes: *The Economic Consequences of Mr. Churchill*, p. 9. These remarks apply *mutatis mutandis* to Indian conditions as they were affected by the stabilisation of the ratio at the higher rate and serve to explain the mill-owners' point of view.

† In his Minute of Dissent Sir Purshottamdas has referred to the view of Mr. J. M. Keynes that in a country like the United Kingdom about two years is the necessary period for readjustment to a 10 per cent variation in exchange, and that if this is the case in a country the bulk of whose trade is external, the period required must be undoubtedly longer in a country like India whose internal trade is much greater in volume than her foreign trade. See para 80.

At the same time, however, we hold that the time is now definitely past for re-establishing the old ratio. The mere fact that the rate has been maintained at 1s. 6d. for over 4 years creates a strong presumption that conditions have settled down to it in a preponderant degree, and that it would probably involve excessive economic disturbance if the ratio were to be changed over again. The 1s. 6d. rate has been too long on the throne to be regarded any longer as a mere upstart and usurper. By right of prescription it must now be looked upon as having acquired 'the divinity which hedgeth a king' and which renders him inviolable. The argument about the sanctity of a well-established standard now belongs of right to the ratio of 1s. 6d. rather than to 1s. 4d.

§ 20. A Central (Reserve) Bank for India :—A feature of the Gold Bullion Standard as proposed by the Commission is the establishment of a Central Bank as the Currency Authority which is to be entrusted with the working of the Standard and control over currency and credit. It is to take over the note issue, manage Government remittances and act as a true banker's bank. The absence of concentrated control over currency and credit and the wasteful duplication of reserves were, as we have already seen, among the defects of the Gold Exchange Standard System. Monetary stability as well as healthy banking development need for their realisation a powerful and well-devised Central Bank. The nature of the proposals made by the Commission in this connection and the various issues arising from them have been dealt with in the chapter on Banking.

§ 21. Restatement of the main points against the Gold Exchange Standard :—In a famous speech which Sir Basil Blackett delivered at Calcutta in December 1926 he summed up the case for 1s. 6d. in 11 points. One of these points was that "no one ratio for the rupee can possibly be permanently more advantageous for India than another." By way of corollary from this he proceeded to deduce in his next point that, "all arguments based on the belief that the fixation of a particular ratio is definitely and permanently advantageous or disadvantageous to this or that interest

are entirely irrelevant." In spite of the temporary nature of the benefits or losses from the ratio, it became the subject of one of the fiercest controversies in recent Indian history, and for a long time it monopolised the attention of the public as well as the Legislature. The more important recommendations of the Commission relating to the change in the standard and in the methods of currency and credit management were thrust into the background. Before attempting to appraise the value of these recommendations of more permanent interest than the ratio it may be useful to collect together at one place the principal points against the Gold Exchange Standard on which the Commission pronounced on the whole an unfavourable verdict. The Commission omit to mention some of the important defects of the old system and gently glide over others which however require to be more strongly emphasised. § It need scarcely be remarked that in criticising the Gold Exchange Standard we do not refer to any ideal system as it might be, but to the system as it was actually worked in India.

§ 22. Reserves and Balances:—First of all we shall notice the shortcomings of the system with reference to the Reserves and Balances. We have already seen how the reserves and the balances created for a particular purpose were indiscriminately utilised for all sorts of purposes (see p. 350). An extreme instance of this was the diversion of a part of the profits on the coinage of rupees in 1907, rightfully belonging to the Gold Standard Reserve, for capital expenditure on railways. The utilisation of the reserves and balances was never governed by a consistent policy, with the result that they were sometimes treated separately and at other times mixed up thus causing a great deal of confusion.

We shall now discuss the question of *the composition of the Gold Standard Reserve*. The Chamberlain Commission pointed out that the position as regards the composition of the Reserve characterised by its investment mainly in long-term securities and by only a small part of it being held in a liquid form was unsatisfactory. They therefore recommended, as already pointed out, † that a larger portion of it should be held in a liquid form and

§ See pp 399-401 above.

† See page 356 above.

in easily realisable securities and that the silver branch of the Gold Standard Reserve should be abolished. As we have already seen the latter suggestion was carried out by Government, but the other recommendations could not be given effect to owing to the outbreak of the War. During the War almost the whole of the Reserve was held in securities in London, and British War Bonds and Treasury Bills were purchased. The recommendation that the securities should be easily realisable was carried out by investment in short-term securities.

The Smith Committee, as already indicated,* recommended that it was desirable to hold a considerable proportion of the Reserve in gold, although they recognised that this was not possible under the abnormal circumstances then prevailing. They also recommended that the securities should be short-term securities issued by the Governments within the British Empire other than the Government of India.

The present position of the Gold Standard Reserve is that it is held in London very largely in short-term paper of various kinds. Recently, however, there has been a slight improvement in the composition of the Reserve in that about £ 2 millions are held in gold as may be seen from the following figures.

Details of the balance of the Gold Standard Reserve on 31st March 1928.

In England—

¶ Estimated value on 31st March 1928 of the	£
sterling securities of the nominal value of	
£ 37,675,352	... 37,843,638
Gold	... 2,152,334
Cash at the Bank of England	... 4,028
	<hr/>
Total ...	£ 40,000,000

Location of the Reserve:—A great and long-standing grievance with regard to the Reserves has been their location in London rather than in India. Most of the Gold Standard

* See p. 372 above.

¶ For details of investments see Report of the Controller of Currency, 1927-28, Statement VI.

Reserve and a part of the Paper Currency Reserve were placed in London. The Chamberlain Commission justified the location of the Gold Standard Reserve in London on the ground that London was the clearing house and the loan market of the world. Further, it was urged that India's principal customer was the United Kingdom and London was the chief place where money was required both for the expenditure of the Secretary of State on India's behalf and for the payment of India's commercial obligations to England and the world in general. If the Reserve were kept in India, it would have to be shipped to London involving unnecessary delay and expenditure. It was also pointed out that there was no short loan market in India and the location of the Reserve there would be wasteful because it would be unable to earn any interest.

The Chamberlain Commission also pointed out that the practice of holding foreign bills followed by the Central Banks in certain European countries provided an analogy to the Indian system of holding the Reserve in London.*

Neither of these reasons can be regarded as fully satisfactory. These complicated arrangements regarding the location of the Reserve were possibly primarily intended for meeting situations of exchange weakness caused by an unfavourable balance of trade. It is, however, very rarely (about once every ten years) that India has an un-

* Prof. Kemmerer however objects that there was really no resemblance between the Government of India selling Reverse Councils on its London Reserves and European Banks holding foreign bills. In selling Reverse Councils "The Government sells drafts against its foreign gold credit (i. e. its gold reserve), when money at home is relatively redundant, as evidenced by exchange having reached the gold export point. Thereby it relieves the redundancy through the withdrawing from circulation and locking up the local money received in payment for the drafts. Under the practice of holding the foreign bills to protect the money market the Central Bank sells its foreign bills when money at home is relatively scarce, as means of securing gold for importation or preventing its exportation. In the former case, the sale of drafts takes the place of an exportation of gold, and the resulting withdrawal of local money from circulation is in essentials an exportation; in the latter case the sale of the drafts abroad is part of a process for securing gold for importation, or for preventing its exportation." Quoted by Ambedkar, op. cit. pp. 172-3.

favourable trade balance, and therefore, it is difficult to see the utility of maintaining these elaborate standing arrangements to meet what was after all a distant contingency.

The advocates of a gold standard for India also hold that the problem of maintaining the exchange is capable of being much more satisfactorily solved by keeping the number of token rupees strictly limited and by introducing a gold standard of the orthodox pattern, under which the notes would be made payable in gold. This would increase their circulation and facilitate the building up of a strong gold reserve for the support of exchange.

The point as regards the requirements of the Secretary of State may be dismissed as trivial. It is quite obvious that the Secretary of State could easily put himself in funds for meeting his expenditure without the Reserve being kept in London for this purpose. The main object of the Reserve is clearly not the convenience of the Secretary of State in this respect.

As regards the absence of a short loan market in India, it is not true that there is no scope for short-term investment in this country, as the experience during the War and after has proved. In any case, interest cannot be considered to be a decisive factor in determining the location of the Reserve.

It is noteworthy that other countries, even if they have an unfavourable trade balance as the normal feature of their international trade, do not usually maintain a reserve at foreign centres. There is no such reserve, for example, kept by any foreign country in India itself on the ground that year after year it has to make payments to India in settlement of trade obligations.

With regard to the *Paper Currency Reserve* it is an anomalous position that the reserve intended for securing the convertibility of the notes circulating in one country should, instead of being kept there, be to any extent located at another place 6000 miles away thus impairing the confidence in the note issue. One of the reasons given for this practice has been that London is the cheapest and best organised market for silver, for the purchase of which it was convenient to hold ample funds in hand. The answer to this contention is twofold. First that England is not

herself a producer of silver and there is no reason why an equally efficient market for the metal could not have been developed in India if Government had consistently made their purchases in the country itself. Instead of making any attempts in these directions Government actually impeded the development of a silver market by the imposition of an import duty on silver. The second answer is that even supposing that purchases were to be made in London there was no particular harm in transferring funds from India when they were actually wanted instead of holding them therein advance. The inconvenience and additional expense would have been well worth while as tending to allay popular suspicion and discontent. It would also seem that in circumstances of urgency, arrangements could have been made for raising the necessary funds in England, e. g., with the assistance of the Bank of England, pending the transfer of money from India. Another evil which was the cause of much popular criticism was the secrecy in which the dealings in connection with the purchases of silver were shrouded.

§ 23. Management of Remittances:—As we have already seen, the sale of Council Drafts by the Secretary of State was the machinery employed for drawing funds from India to London. The complaint in this connection was that unnecessarily large amounts were transferred from India to London by this method, especially since 1904. The reasons given for this were often puerile in character. It was said, for example, that this system enabled the Secretary of State to strengthen his financial position without explaining why such strengthening was needed. Similarly, it was said that it was desirable that the Secretary of State should avail himself of exceptionally profitable rates for the Council Bills whenever they could be obtained. Here again the assumption is tacitly made that the question whether the funds were required was of subordinate importance. It was often claimed that by drawing more money than was immediately required for his expenditure the Secretary of State made possible an avoidance or reduction of debt. But these excessive drawings encouraged the policy of surplus budgets in India. Instead of the avoidance or reduction of debts, remission of taxation in India would have

been a more worthy object to pursue.* Besides it was noticed that even when the Secretary of State's cash balances were ample, large floating loans were raised in London.

The superfluous money which accumulated in the hands of the Secretary of State in this manner was loaned out in London at very low rates of interest to "approved" borrowers, of whom a list was maintained by the Secretary of State. Complaints were common that a good deal of favouritism was shown in the administration of these loans, and colour was lent to these complaints by the fact that the members on the Finance Committee of the Secretary of State's Council were often themselves Directors and businessmen who were interested in selecting the recipients for these loans.

Another practice that was objected to was that the Council Bills were often sold at rates below the specie import point even when there was no urgent necessity for funds in London.

One of the principal justifications, that was commonly given of the sale of Council Bills beyond the requirements of the Secretary of State was that it was a great help to the foreign trade of India. But the trade was fully capable of looking after itself and would have had no difficulty in finding alternative means of financing itself, as in fact it has done with sufficient ease whenever the sales of Council Bills happened to be curtailed for some reason or other. There was thus no overwhelming reason why Government should have gone out of their way to assist trade. All that they need have done was to make gold freely available for export whenever required.

The Chamberlain Commission combated the suggestion that the sale of Council Bills served to mitigate the seasonal monetary stringency in India. It pointed out that the demand for money arises in the first place from the necessity of financing the movements of crops up-country, but Council Drafts are taken only when the produce is ready for export; there is thus an important period during which the needs of the market are not met by this means. "It is obvious also," the Commission go on to remark, "that

* See Sections on Public Debt in the Chapter on Finance.

the sales of Council Drafts are affected by circumstances quite independent of the Indian money market; a high Bank Rate in London, for instance, or the holding back of produce in India for higher prices may result in the demand for Council Drafts being slack in the busy season, while revenue collections are as heavy as ever. In this case the money so collected accumulates in the Reserve Treasuries and remains locked up there." This incidentally leads us to remark that while India's money was loaned out in profusion for the benefit of the money market in London, it was locked up in the Government Treasuries in India when the money market there was thirsting for accommodation and the bank rates that ruled were extortionate.

The Council Bill system had all the appearance of an elaborate device for diverting the flow of gold from India and save London the inconvenience and cost of finding it for India "while acting as a receptacle for as much of India's gold as possible—not to hold but to use."*

In his memorandum to the Babington Smith Committee, Sir Stanley Reed pleaded forcefully for an abolition of the control over the Indian exchanges exercised by the Secretary of State. He urged that the Government of India, and, to no less a degree the Secretary of State, were suspect in the eyes of a large section of the Indian community. The Secretary of State, he pointed out, operated 6,000 miles from the great Indian financial centres. "He was surrounded by, and naturally amenable to, interests not Indian in their ideas and aims. He acted in secret, and it was frequently impossible to obtain any information in India of the groundwork of measures which, however wise and expedient in themselves, were not understood and were liable to perversion in India. The political disadvantages of such complete powers being exercised in secret so far from the people vitally affected by them could not be easily exaggerated." Sir Stanley Reed therefore, concluded that the only remedy was for the Secretary of State to divest himself as completely as possible of the management of the Indian Currency and exchanges.

*See *Indian Currency and Finance*, (The Times of India, 1913), p.57. This is a useful collection of a series of articles in the Times of India dealing with various phases of the currency and exchange controversy before the War.

The objection to the Indian system was thus not that it was managed, for in most civilised countries management in some form or other is essential, but that it was ill managed or at least such was the widespread opinion held about it by the great majority of the Indian people who gave any thought to these matters. In the words of Professor Nicholson, "It is a bad thing for a country when the masses of the people begin to feel that something is wrong with the currency," and, whatever the inherent excellences of the Gold Exchange Standard, it certainly had made the people of India think that something was very wrong with their currency system.

§ 24. Inflation of Currency and rise of prices:—The Hilton Young Commission as we saw pointed out that the Indian system was unautomatic (see pp.399–400) and was especially defective on the side of contractibility of superfluous currency. One of the inevitable results of this was an inflation of currency with its attendant evil of an excessive upward movement of Indian prices.* As Professor Nicholson pointed out in his criticism of the Report of the Chamberlain Commission, since the convertibility of the rupee was partial and often suspended, it was unavoidable that in course of time, if new additions continued to be made, the cumulative effect must come into operation causing a general rise in prices, and there can be no doubt that the inflation of currency brought about in this manner has been the principal cause of the phenomenon of rapidly rising prices during the last quarter of a century or so.

With the best intentions in the world, Government was liable to grave errors of judgment in ascertaining the currency requirements of the country.‡ The demand for rupees often

* See Chapter X on Prices.

§ " Here in India, Government has been attempting too much; it has taken upon itself the whole task of providing the necessary supply of currency, and adjusting it to varying needs of different occasions—a task not completely entrusted even to a banking institution in any other great country of the world—a task beyond its ability and one that exposes it to undesirable pressure...In fact since the closing of the mints the Indian currency system has been managed at the whim of the latest official sent out

appeared to be quite sound and necessary without its really being so, and misjudgments were particularly easy as the rupees once issued to the public went up-country and did not come back quickly.

§ 25. A haphazard and expensive system:—The Gold Exchange Standard in India had resulted from a series of administrative notifications not consistently informed by any deliberately adopted ideal. Many of the practices that had come into vogue as integral parts of the system had no legal validity. As Mr. Dalal remarked in his Minute of Dissent (paras 59–60), the system as a whole was never clearly and explicitly defined and this had a general unsettling effect.

The Gold Exchange Standard was often commended for its cheapness relatively to a gold standard proper. But if we allow their proper value to all its disadvantages as detailed above, it would be excusable if we concluded that the cheapness of the system was very dearly bought indeed!

The system had failed to educate the people and teach them to appreciate the benefits of economical forms of currency. On the contrary, as has often been pointed out, the Gold Exchange Standard has encouraged the hoarding habit among the Indian people* and has intensified their desire for a gold standard with a gold currency inspite of its expensiveness as being the only safe and reliable system.

§ 26. Internal vs. external stability:—In order to be quite fair to the Gold Exchange Standard, we must count its successes as well as its failures, its hits as well as its misses. One of the achievements with which it has been credited has been that it gave the country a long period of exchange stability. Of course it broke down utterly during the war, but this happened to almost every other currency in the world. And on the whole,

from England. ' One man could come along and stuff the currency, the next would starve it there has been no plan at allbut always some fresh experiment advised—a gold mint, prohibitive duties on silver bullion—anything or everything.' (Moreton Frewent's evidence before the Chamberlain Commission.) See Chabiani: *Indian Currency and Exchange*, pp. 164–65.

* See page 401 n.

we think that the Gold Exchange Standard succeeded in keeping the foreign exchanges more stable than under the silver standard. We must, however, hasten to add that not all its critics are inclined to admit even so much. They point out that even if the war period is excluded from consideration the system could not be said to have stood the test proposed for it. The only time that it was put to the proof before the war was during the crisis of 1907-8 and then the system was kept standing only with the help of outside supports. Government had to give an undertaking to borrow, if this was necessary, to maintain the standard and were compelled to increase taxation in order to lay down gold.* The system therefore was only a fair weather system and it threatened to collapse at the least little sign of a storm.

However, even if we admit that prolonged stability of exchanges was one of its positive achievements we must put against this the internal instability of prices with a general tendency towards a rise which, as we already have remarked, it occasioned. Most economists agree that stability of internal prices is far more important than stability of the foreign exchanges. In any case, the Gold Exchange Standard system was not the only possible way of obtaining stability of exchanges. One of the recognised merits of a gold standard system is that it is capable of yielding simultaneously the advantages both of stable prices and stable exchanges. But it was not adopted in spite of the incessant clamour for it on the part of the public.

GOLD BULLION vs. GOLD CURRENCY STANDARD

§ 27. Critique of the Gold Bullion Standard:—Before proceeding to criticise the most fundamental of the recommendations of the Commission about the Standard, we may emphasise the importance of the great task of monetary reconstruction entrusted to the Commission. In the words of Sir Stanley Reed, "The responsibility remitted to the Commission was not the mere stabilisation of the rupee, but the establishment of the standard which would command reasoned confidence in India, to link the rupee to that standard, and to provide for its satisfactory control, automatic working and stability; to bring the control of

* Times of India articles on Indian Currency and Exchange, 1913.

currency and credit under a single authority and to free the Indian Currency and Exchange system from the dominance of the silver market. In short, it was to establish the rule of law in place of the practice of administrative discretion." * The Commission's criticism of the Exchange Standard was cogent and effective so far as it went. They rightly argued that a backing for the internal currency more solid, simple and certain than provided by the existing system of Exchange Standard was needed to win public confidence and to promote the banking and investment habits, and that in the existing state of public opinion in India such backing could only be in the form of gold. They claimed for the Gold Bullion Standard which they advocated that it made gold the sole standard of value and ensured the absolute convertibility of the internal currency into gold for all purposes, though it so arranged matters that while gold was to be always available in exchange for currency in India, that gold would remain in the central reserves for use in supporting the exchange value of the currency, but would not go into circulation. § The latter object was to be fulfilled by the demonetisation of the sovereign and the sale by the currency authority of gold in the form of bars. Its purchase from the same authority by the public for non-currency purposes was to be guarded against by offering gold in quantities of not less than 400 ounces (or 1,065 *tolas*) at a time and at a rate inclusive of the cost of importing gold from London to Bombay. (See page 409 above.)

The convertibility of legal tender currency into gold bars may be good enough for banks and bankers but it is hopelessly inadequate and unintelligible to the masses. Also the minimum limit of 400 ounces is excessive and impedes the convertibility into gold so as to make it unreal. † The demonetisation of the sovereign and half-sovereign has been widely criticised as a

* See Indian Year Book, 1927, p. 302.

§ Sir B. Blckett's Delhi Speech, Nov. 23, 1926.

† The minimum limit for buying and selling was reduced in the new Reserve Bank Bill (published in January, 1928) to 250 *tolas*. This Bill, as we shall see later on, was not allowed to be moved in the Assembly, but the reduction of the minimum proposed therein shows that the original limit was felt to be too high. The lower limit was first suggested by the Joint Committee on the original Reserve Bank Bill.

definitely retrograde step, since even under the Exchange Standard before the War, a considerable number of sovereigns, estimated at £ 60,00,000 were in the hands of the public. The objection that gold sovereigns would be imported from abroad and pass into circulation without any control by the currency authority could be met by the issue of an Indian Mohur.

§ 28. Case for a Gold Currency Standard in India:—The Commission's scheme of the Gold Bullion Standard has obviously been influenced by the analogy of the English system. The restoration of the gold standard in the form of a bullion standard in England in 1925, it is said, marks a considerable advance in the world's currency evolution towards the ideal system of an International Exchange Standard as adopted by the Geneva Conference in 1922, under which the internal currency would consist of inconvertible paper and gold would be available only for liquidating foreign debts.

It must, however, be remembered that even England had the gold currency standard before the War, and it was more by force of circumstances than from choice that she has adopted the Gold Bullion Standard. It is hoped and expected by currency reformers that, after having experienced the benefits of the Gold Bullion Standard, England may not desire to go back to the gold currency even though she may be able to do so in the future. But it may be pointed out that what suits an advanced nation like England may not suit a backward country like India. The English people are far better educated and they have a far greater confidence in the currency authority than the people in India. Also, in England, under the old system of gold currency standard, there has been a great development of banking and investment habits among the people. In India, on the contrary, thanks to the vagaries of the Gold Exchange Standard and of its official management, public confidence has been impaired and the hoarding habit has been encouraged. The people are inclined to look askance at "refined and logical currency systems" and prefer the cruder but well-tried system of a gold standard. Moreover, the persistent refusal on the part of the authorities to satisfy the demand for a gold

currency has added to the strength of the desire for it. Nothing short of a visible gold coin in circulation and the convertibility into it of all other forms of money will convince the people that they have an effective gold standard. Most people in India are incapable of going through the intellectual gymnastics required for grasping the conception of a gold rupee as equivalent to 8.47 (or, to be more exact, 8.4751) grains of gold. The Commission's proposal in regard to the certificates payable in gold bullion * is not likely to be entirely satisfactory for the purpose of demonstrating to the people the solidity of the gold basis. It may not be true that a gold currency is an absolutely necessary stage through which every country must pass before it can attain to an ideal standard of which economists have dreamt since the time of Ricardo. But we hold that under the existing conditions in India a gold currency cannot be regarded as an unnecessary luxury or a mere matter of traditional etiquette associated with the gold standard. This is why almost all Indian witnesses and some European witnesses of unquestioned competence like Dr. Cannan strongly urged on the Hilton-Young Commission the need for the adoption of a gold currency standard and Sir Basil Blackett himself expressed the view (in his Delhi speech) that, before India could think of any ideal system she would probably have to pass first through the stage of having gold coin available, into which all other forms of currency would be convertible at will.

The gold currency standard is by no means a perfect standard or the last word in currency wisdom. It can obviously be very expensive, and although it is preferable from the point of view of stability of prices to a gold exchange standard as we have known it in India, it does not give us as much of immunity from price fluctuations as we might desire. As Dr. Cannan observes, "to tie the purchasing power of money to that of a single metal, though that metal is a very fine one, which would be put to an immense number of uses if it were less scarce than it is, has been rightly described as an expedient fit only for a barbarous age."† Many novel schemes promising a more perfect

* See p. 411 above.

† See *Economic Journal*, June, 1924, p. 161.

stability than is possible under a gold standard are being suggested and progress no doubt requires constant though cautious experimentation undertaken to test the practical utility of the new doctrines instead of allowing them to slumber "in the dormitory of the understanding." But it is generally believed that, before any such experiments could be tried with a reasonable chance of success, it is first necessary for all the countries to put themselves on a firm gold basis. "When the golden thread runs between all the nations of the world"* it would be easier for them to introduce higher forms of currency regulation. The exact type of a gold standard to be adopted by any given country will of course depend on its special conditions. And, as we have already pointed out, the present conditions in India require a gold standard with its usual concomitant of a gold currency. The simplicity and intelligibility, which the Commission admit as being indispensable requisites of any currency system that could be regarded as satisfactory for India, cannot be said to be the distinguishing features of the Gold Bullion Standard recommended by them.

§ 29. Other objections to the Commission's proposals:—The buying and selling rates of gold proposed by the Commission have also been subjected to unfavourable comment. The regulation of the rates in such a manner that the currency authority will buy gold when it is cheapest and sell it when it is dearest in the market will have the effect of making the buying and selling transactions rare in India. This applies especially to the sale of gold by the currency authority. The public will buy only when the purchase is necessary for export purposes. Further, the offer to sell gold at a more favourable rate in London than in Bombay proposed by the Commission when exchange is below the upper gold point would encourage, or perhaps is intended to encourage, the delivery of gold in London. This has been objected to as perpetuating one of the evils of the Gold Exchange Standard.† In this connection we may refer to

* D. M. Mason: *Monetary Policy*, 1914-28, p. 108.

† See Junnarkar: *An Examination of the Currency Commission's Report*, p. 55.

the Commission's recommendation that "of the (Reserve) Bank's holding of gold coin or bullion, at least one-half shall be held in the Bank's custody in India, while the remaining half may be held outside India in the custody of its branches or agencies or deposited in other banks earmarked for the Bank's account. Gold in any mint or transit belonging to the bank shall be counted as part of its reserves". (para 145). The large holding of gold securities recommended by the Commission means that our reserve to that extent will be invested abroad. In view of the suspicion and distrust which the practice of holding reserves in London has engendered, special care was necessary not to propose any arrangements which would involve the location of Indian money in London. That the suspicion and distrust still persist is brought out by the fact that the non-official majority on the Joint Committee to which the Reserve Bank Bill (1927) was referred, insisted on introducing a clause that at the end of ten years, at least half the gold assets in the new reserve should consist of gold coin or bullion with a view to ensuring the free inflow of gold into India, which otherwise might be intercepted by the substitution of gold securities for gold coin or bullion. They also insisted that 85 per cent of the gold coin and bullion in the total reserve should be held in India.* Apart from the question of public confidence in currency matters, the transition from the Gold Bullion to the Gold Currency Standard which the Commission are anxious not to impede, if the people desired it, will be rendered difficult if large gold assets are held abroad in the form of securities.

§ 30. Alternative schemes of a gold currency :—The Commission do not seem to have given proper consideration to any other schemes for the introduction of the gold standard than the Blakett scheme. There were several other proposals before them which appeared eminently workable. For example, there was a scheme elaborated by Dr. Gregory which promised the introduction of a full-fledged gold standard at the end of five years without involving excessive cost. There was another scheme proposed by Dr. Cannan† in which he showed how the transition to

* See Report of the Joint Committee on the Reserve Bank Bill, clauses 7 and 8.

† See Appendices 80 and 81.

a gold currency standard could be made in India "without any large risk at any point and at the same time with considerable rapidity." He suggested the following steps for achieving the transition:—(a) At once open the mint to the free coinage of gold, the mint to be bound to give as much gold in coin as it received in bullion, less a small charge for cost of manufacture. (b) At the same time declare the new coins and equivalent old ones, if any, to be legal tender (unlimited) as rupees at the ratio fixed. (c) At the same time suspend all additional issue of silver coin, and stop all additional issue of notes redeemable in silver. (d) Then make the notes convertible into gold coin at the option of the holder, but proceed by instalments, taking first the notes of largest denomination, and proceeding downwards, class by class, very rapidly if no demand appear at each stage, till all the notes are convertible into gold. (e) Then apply the same method to the silver rupee, taking them in instalments, beginning with those of most recent date.

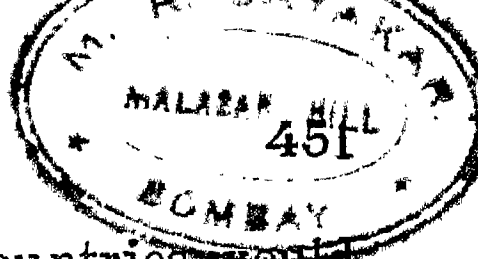
§ 31. Gold currency not impracticable:—In this way Dr. Cannan thinks that complete convertibility of silver coins and notes into gold could be introduced in the course of a single year without causing any appreciable demand for gold. "The overwhelming majority would not become aware that any change was going on, and those who knew about it would have no reason for taking any action." There is no reason to fear that an inconveniently large number of rupees would be presented for conversion into gold. The Commission most probably overestimated the stock of surplus rupees like the scheme of the Finance Department which also gave an exaggerated estimate in order to err on the safe side. If no attempt is made to limit the legal tender quality of the rupee there is no particular reason why people should be anxious to convert their rupee hoards into gold. As Dr. Cannan puts it, "to bring them out would be inconvenient to the owners owing to the risk of publicity and robbery and nothing would be gained by it except some saving in the space which is really quite negligible in the case of hoards already made."

Gold coins may at first be preferred to notes, but there is no reason to suppose that this would be anything more than a temporary phase. Besides, notes would always be preferred for bank cash reserves and for remittances. On the other hand, when they are made unconditionally convertible into gold there is every chance of their increasing in popularity. As the existing stock of rupees becomes gradually absorbed in circulation with increasing demand for currency it should not be difficult to lay down sufficient gold to be held as a reserve against notes. Further, it may be expected that part of the large amount of gold which is imported into the country year after year in liquidation of the balance of trade would be presented for obtaining currency. The gold reserve could also be gradually strengthened by the redemption of the English securities in the Gold Standard and the Paper Currency Reserves. Lastly, the gold that is at present hoarded is likely to come out, especially if the necessary steps are taken to hasten the development of banking organisation in the country.

§ 32. The attitude of Europe and America:—As regards the hostile attitude of other nations, which the Commission think is bound to make futile any attempt to introduce a gold currency in India, this will depend on the amount of gold India is likely to absorb. Dr. Gregory and other authorities do not anticipate that the Indian demand will be so huge as to cause any considerable unsettlement in the gold market of the world.

We are told that Europe and the United States are anxious to guard themselves against the scarcity of gold supplies to be expected in the future and the consequent fall of prices. But this is not a view which has been universally accepted. Prof. Irving Fisher, for example, thinks that the danger to be feared is rather that prices will go on rising to an inconvenient extent. Dr. Cannan also is of opinion that although prices will fall as the immediate result of the restoration of the gold standard in the European countries, the old rise would soon be resumed.* The same writer has argued that the adoption of a gold standard

* See Edwin Cannan: *An Economist's Protest*, p. 229.



by India instead of injuring England and other countries would in fact benefit them. After being accustomed to a paper currency they are not likely to return to gold coins. Moreover, "the superstition that immense cellarfuls of eternally idle gold are necessary to 'back' or 'support' the value of paper currency is, like other superstitions, losing strength," so that the Central Banks in the Western countries will tend to hold smaller gold reserves than heretofore. Consequently, if the East takes no more gold than before there is a great danger of gold depreciating, i. e., prices rising in the gold standard countries. Additional demand from the Eastern countries, therefore, provided it is on a moderate scale, is to be welcomed rather than feared by the Western countries. India has thus apparently still a useful role to play as a sink for absorbing the redundant bullion of the world. The redundancy, however, being no longer excessive, she is now exhorted to moderate her demand and to put a curb on her powers of absorption.

§ 33. Effect on silver hoards:—As we have already seen, it has been urged as an objection to a gold currency in India that it would depress the price of silver and consequently the value of the large silver hoards of the masses. That this will be the effect to some extent need not be denied, though its magnitude appears to be exaggerated.* But this argument was equally valid when the mints were closed in 1893. It did not then suffice to stay Government action which on the whole has been regarded as entirely justifiable under the circumstances. It may perhaps also be urged—though we do not care to stress the argument too much—that, although the hoards may be very large in

* With reference to this objection Professor K.T. Shah in his *Sixty Years of Indian Finance*, (2nd Edn. p. 519) attempts to turn the tables on the Commission by pointing out that they themselves did not hesitate to recommend the higher ratio of 18 pence although this meant the depreciation of the value of the silver stores by $12\frac{1}{2}$ per cent. As against this, however, it can be argued that the higher ratio would bring down the price not only of silver but of all other commodities as well. If the value of silver goes down by $12\frac{1}{2}$ per cent in terms of rupees, this would be no hardship because the value of the rupees in terms of commodities would go up to the same extent. The Commission's argument refers to a *probable fall in the value of silver greater in degree than that suffered by other commodities*.

the aggregate, the individual share of the hoards is small and the loss on it will not be felt so severely as the aggregate figure would suggest. Another point, to which again we do not wish to attach too much importance, is that if silver is likely to depreciate, gold is likely to appreciate and for the same reason. The loss on the silver hoards will, therefore, be counterbalanced in same measure by the gain on the gold hoards.

§ 34. Trade with China:—The Commission have made rather too much of the adverse influence on India's trade with China of the adoption of a gold currency by India. But the loss in this connection may be regarded as negligible in view of the very small part which China plays at present in India's foreign trade. It also stands to reason that this loss cannot be anything but temporary as the international exchange of goods is governed in the long run by more permanent factors than occasional changes in the currency policies of the different countries.

§ 35 Need for a gold mint:—We attach great importance to the establishment of a gold mint in India as the clearest outward sign of a gold standard, even if it were only to "flatter an ignorant vanity."* It will remove a long-standing grievance and it will convince, as probably nothing else will, that the foundations of a real gold standard have been well and truly laid. In addition to this the coining of an Indian gold Mohur suggested above will obviate the necessity of any dependence on the British Treasury whose obstructionist tactics in the past and wrong-headed and obstinate opposition to a gold mint in India have not particularly endeared it to the Indian people.

§ 36. Conclusion:—It is no use pretending that the transition to a proper gold standard will be an absolutely painless process. But we should like to apply to the difficulties in connection with a gold standard in India what has been said about the difficulties attending necessary deflation of currency. 'They must be regarded in the same light as those which a spendthrift or a drunkard is rightly exhorted by his friends to face like a man.' After indulging in the prolonged orgy of the Gold Exchange Standard, the nation

* Keynes; *Indian Currency and Exchange*, p. 87.

must consent to go through the more or less painful ordeal of a return to more sober ways in currency matters.

The Commission have done a valuable service to India by recommending that the Gold Exchange Standard, which had been the cause of so much discontent should be definitely scrapped, and that the official control over currency and exchange should disappear utterly and for ever. But they are open to the criticism that in some ways, although they started from the right premises, they arrived at wrong conclusions. The Gold Bullion Standard which they proposed as an effective remedy for all the evils of the gold Exchange Standard and on which they have showered so much praise, has not excited any enthusiasm in the minds of the Indian people. It is, therefore, desirable that if we cannot get along without the Gold Bullion Standard for some time to begin with, it must at least be restricted to a short and definite period with a statutory assurance that the full-fledged Gold Currency Standard would come at the end of it., instead of being left to an indefinite future.

§ 37. Government accept the Hilton-Young Commission's Report:—On 16th January, 1927, Government published three Bills embodying the commission's recommendations. These were (i) a Bill to establish a Gold Standard currency for British India and constitute a Reserve Bank of India, (ii) a Bill to amend the Imperial Bank Act, 1920 and (iii) a Bill further to amend the Coinage Act of 1906 and the Paper Currency Act of 1923 for certain purposes, and to lay upon Government certain obligations in regard to the purchase of gold and the sale of gold exchange. The first two Bills will be referred to in our chapter on Banking. Here we are concerned with the third Bill which was moved in the Assembly by Sir Basil Blackett on the 7th March, 1927.

The Finance Member explained the principle of the Bill, which was that the time had arrived to stabilise the rupee and that the Bill proposed for the first time in Indian financial history to impose a statutory liability on the Currency Authority to maintain the rupee at the ratio thus fixed. Before the War there had been no statutory provision for preventing the rupee from

falling below a fixed ratio of gold so that the link between the rupee and gold was imperfect. Sir Basil Blackett pointed out that the Bill was no more than a transitional measure intended to be operative only during the period between its passing and the time when the Gold Standard and Reserve Bank Act should come into operation. The Bill was bitterly opposed at every stage, but finally passed by a narrow majority with one or two minor amendments after a great and memorable fight. The Council of State passed it without any amendment. The Indian Currency Bill thus became law and came into operation from 1st April 1927.

The new Act established the ratio of 1 s. 6 d. by enacting that Government would purchase gold at the price of rupees 21 annas 3 and pies 10 per *tola* of fine gold in the form of bars containing not less than 40 *tolas*, and would sell gold, or at the option of the Government, sterling for immediate delivery in London at the same price after allowing for the normal cost of transport from Bombay to London. A rate of 1s. $5\frac{4}{8}$ d. was notified as the Government selling rate for sterling to meet these obligations.* On 1st April, 1927, when the Indian Currency Act of 1927 came into force conditions attaching to the acceptance of gold at the Bombay mint were published. As the rupee sterling exchange did not reach the upper gold point in the course of the year 1927-28 no gold was tendered at the Mint. At the beginning of the present busy season, 1928-29, the rate of exchange and the conditions in the money market have been such as to lead to the offer of gold (mostly in the form of sovereigns) in exchange for currency. So far, it would seem that the Gold Standard has actually begun to function and the provision for the automatic expansion of currency is working in practice.

By the same Act, sovereigns and half-sovereigns ceased to be legal tender in India, but an obligation was placed on Government to receive these coins at all Currency Offices and Treasuries at their bullion value reckoned at Rs. 21-3-10 per *tola* of fine gold. i. e. Rs. 13-5-4 per full weight sovereign. The value of the sovereigns received by the Government at this rate during

* Report of the Controller of Currency, 1926-27, p. 3.

the year 1927-28 was only Rs. 5,034. In spite of the fact that these coins have ceased to be legal tender the value of their imports increased from 5,64 lakhs to 6,71 lakhs.* The history of the other two Bills and the fate of the Reserve Bank Bill will be dealt with in the chapter on Banking.

§ 38 System of Government Purchase of Sterling:—When describing the mechanism of Council Drafts attention was called to the recently started practice of Government purchase of sterling and it was remarked that this constituted an important modification of the Council Bill system.† We have also made passing references to the employment of this new method for arresting the rise of exchange beyond a certain desired level.§ We may now conclude this chapter by a more detailed description of this new system, which has been introduced since 1923-24. In that year, while the weekly sales of Council Bills continued as before, the sales of Intermediates at higher rates were stopped and were replaced by the purchase of sterling in India from Banks and private financial houses willing to sell their sterling resources in London for rupees offered to them in India. These purchases were conducted by Government through the agency of the Imperial bank. The system was further extended in 1924-25 when the purchase of sterling was resorted to as the principal method of remittance, the weekly sale of Council Bills being started only when a steady and continuous demand for Council Bills manifested itself. During the year 1925-26 there was no sale of Council Bills and the system of Council Drafts has since then been entirely superseded by the novel method of sterling purchases in India.¶ The Hilton-Young Commission recommended the purchase of sterling by competitive public tender and the publication of the weekly returns of remittances. This recommendation has been adopted by Government, and since April, 1927, the system of purchase in India by public tender has been

* Report of the Controller of Currency, 1927-28, p 5-6.

† See p. 36 n. above.

§ See p. 387 above.

¶ See the Historical Memorandum on Indian Currency by Mc. Watters, submitted to the Hilton young Commission, Vol. II, p. 22.

inaugurated. Tenders are received on one day each week, usually on Wednesday, simultaneously in Calcutta, Bombay, Madras and Karachi, and particulars of the amount allotted at each rate, if any, are published on the following day in each of these places. Between the days on which the tenders are received intermediates are on offer at the offices of the Imperial Bank of India at these places at a rate $1/32$ d. above the highest rate accepted on the previous day on which the tenders were received.* The weekly returns of remittances are also published as recommended by the Hilton-Young Commission. As in the case of Council Bills the system of sterling purchase enables the Government to take advantage of a firm or rising exchange and also to prevent the appreciation of the rupee above the point fixed by Government.† The object underlying the new system is that the factors influencing the immediate course of exchange can be much more accurately and promptly judged in India and the purchases can be regulated much more satisfactorily with reference to the varying conditions of the market. The operations of Government can be conducted so as to avoid violent fluctuations in the rate with benefit both to trade and to the country in general. In the early part of 1924-25, as we have already seen, the upward rise of exchange was prevented by Government purchases of sterling when the exchange had reached 1s. 6d. Since then Government have been able to keep it comparatively stable at that point by their readiness to purchase large sums in sterling near this rate.§ This method suits the Exchange Banks very well for they need no longer depend on re-discounting their bills in London as they can sell them to the Government of India and immediately replenish their funds in this country.¶

The disadvantages attendant upon this system are similar to those which were usually made a ground for criticising the old

* See Report of the Controller of Currency, 1927-28, p. 9.

† When the exchange tends to be weak, the method of Reverse Councils will have to be resorted to as before.

§ During 1927-28, Government purchases of sterling amounted to £ 28.32 millions or Rs. 37.77 crores and were made at an average rate of 1s. 5.997 d.

¶ See Sections on Exchange Banks in the chapter on Banking.

Council Bills system. For example, it is possible for Government, unless they take care to limit their purchases of sterling to their actual requirements, to increase their magnitude to such an extent as to prevent in a large measure the free flow of gold into India. Similarly, the rate of purchase can be regulated in such a manner as to produce the same effect. If Government offers rupees at lower rates than the upper gold point, the flow of gold will be effectively diverted from India. Another disadvantage that has been pointed out relates to the sale in India by the public tender system which places foreign centres dealing with India at a disadvantage. Under the old system, because the Council Bills were sold in London which was the world's financial centre, foreign countries could easily compete in the purchase of Drafts on India. It is more difficult for the foreign demand for rupees to manifest itself equally easily in India and thus Government may not be able to obtain the best possible price for the rupee. Most of these evils, however, will be obviated if a Central Bank is started and made entirely responsible for the remittances to the Secretary of State on behalf of the Government of India, and to maintain the stability of the exchange. It is essentially a question of replacing Government agency by a more competent agency such as the proposed Reserve Bank. The machinery of purchase of sterling is in itself an advance over the Council Bills system for reasons mentioned above, but its operation is likely to be more efficient and less liable to public criticism, if the proposed Reserve Bank rather than Government were to take charge of it.*

* Cf. Article on Purchase of Sterling by Ramchandra Rau, Mysore Economic Journal, June, 1928.

CHAPTER X

RISE OF PRICES IN INDIA.

§ 1. Importance of the problem of prices:—Problems connected with price movements are at once the most abstruse and the most important in the discussion of economic conditions in any country. The importance of understanding the nature and extent of price movements is clear from the fact that Land Revenue assessments are largely based on them in this country. Price changes have also been associated with Government's currency policy in India, and the question whether they indicate increasing prosperity or the reverse has been the subject of endless and acrimonious debate. An attempt will, therefore, be made in this chapter to measure the price movements in India in recent years and to ascertain their significance.

The movements of prices in India began to attract notice in the early seventies of the last century owing to the depression of industry and trade in gold standard countries and the striking fall in the value of silver which, as we saw, began from about 1874. Towards the end of the 19th century, much controversy had arisen regarding the relative stability of prices under the different standards. The general impression was that prices had been much more stable in the silver standard countries like India than in the gold standard countries, and it was in order to test the validity of this impression that Mr. F.J. Atkinson worked out figures bearing on price movements in India since 1861 in his "Silver Prices in India from 1861."* It is, however, since the opening years of the present century that discussions regarding the tendency of prices to rise continuously have figured prominently in Indian economic literature. There was a widespread feeling that the continued rise of prices urgently called for investigation and it was held by the critics of Government supported by

* See Vakil and Muranjan, *op. cit.*, pp. 134-35.

the late Mr. Gokhale * that the currency policy of Government was largely responsible for the evil. In 1910, the Government of India decided to undertake an exhaustive enquiry into the subject and entrusted the task to Mr. K. L. Datta of the Finance Department assisted by Mr. Findlay Shirras and Mr. S. D. Gupta of the Finance Department. The Report of this committee was issued along with the Resolution of the Government of India in October, 1914. Before proceeding to deal with the findings of the Committee we may say a few words regarding the general trend of prices before the year 1890, which was chosen by the Committee as the opening year of the period (1890-1912) over which their enquiry extended.

§ 2. A bird's-eye view of price movements since 1861:—The table given below indicates the general course of prices in India since 1861 with 1873 as the basic year. * The General Index Number is based on the wholesale prices of 39 articles (28 exported and 11 imported articles) except in the case of food grains, viz. Jowar, Bajra, barley, Ragi and gram—wholesale prices of these articles not being available before 1897.

The Government Index Numbers issued in the publication "Index Numbers of Indian Prices" in column two of the table are unweighted. The equal importance attached to the commodities prevent the Index Numbers from faithfully recording the nature and extent of the changes in the price level. India is an agricultural country and her agricultural production which accounts for the bulk of her total production consists of a few staple commodities like rice, wheat, cotton, jute, etc., while others are comparatively insignificant. Some articles like cotton cloth, cotton yarn, raw silk and coal have been allowed to exercise an undue influence upon the final result and the whole series of

* See Speeches of G. K. Gokhale, pp. 150-153.

† The year 1873 was chosen as the basic year because of normal seasons and because it was since about that year that the depreciation of silver and the consequent depreciation of the rupee may be said to have started.

prices is dominated by imported goods and those in direct competition with them.*

Year	General Index Number for (39) articles (unweighted)†	Weighted Index Number (100 articles) equated to 100 for 1873‡	General weighted Index Number for 33 articles.¶
1861	90	93	86
1865	107	109	117
1870	102	107	107
1875	94	96	103
• 1880	104	126	113
1885	87	106	99
1890	100	117	113
1895	104	120	109
1900	116	143	112
1905	110	135	121
1910	122	150	129
1913	143	182	159
1914	147	187	164
1915	152	182	158
1916	184	185	177
1917	196	186	193
1918	225	215	231
1919	276	301	295
1920	281	302	378
1921	236	273	...
1922	232	266	...
1923	215	259	...
1924	221	257	...
1925	227	265	...
1926	216	260	...

*See Vakil and Muranjan, op. cit, p. 140.

† See *Index Numbers of Indian Prices* (1928). The weighted index number set out in the third column of the above table was originally constructed by Mr. F. J. Atkinson of the Indian Finance Department. The index numbers for the years subsequent to 1909 have been compiled by the Department of Statistics on the lines of his calculations. For further details see Appendix C, p. 22, *Index Numbers of Indian Prices* (1928).

¶ Index Numbers in this column are taken from Vakil and Muranjan : op. cit. pp. 308-309.

§ 3. Period from 1861 to 1893 :—We indicate below the general character of the price movements between 1861 to 1893.*

(i) *Rising Prices* (1861-1866) :—The American Civil War led to a scarcity of cotton. The resulting high prices caused a great influx of specie into India and extensive coinage of silver which was followed by a considerable rise of prices. This episode of high prices showed clearly for the first time the influence of external factors on the price level in India.

(ii) *Falling prices* (1866-1883) :—Except for a sudden jump in the prices of food stuffs between 1876 and 1879 due to the great famine which especially affected Western and Southern India, prices were falling from 1866 to 1883. This general fall in the earlier years may be regarded as a reaction against the previous high prices, and in later years as a counterpart of the general downward movement of prices which began in the Western countries from about 1874. It has been attributed to the slackening in the production of gold, the adoption of the Gold Standard by countries previously on a silver standard basis, the arrest of the expansion of the silver currency owing to the closure of the mints to its free coinage, the slowing down of the development of banking and the growing volume of trade under the stimulus of a decrease in the freight charges and improvements in the arts of production.†

(iii) *Rising Prices* (1883-1893) :—The fall in prices in India was arrested earlier than in the gold standard countries of the West, as a result of the depreciation of the rupee. It must be noted, however, that though silver began to depreciate in terms of gold roughly since 1874, the general increase in the production of commodities led to a fall of prices until about 1883. Since 1885 the production of silver definitely outstripped the production of commodities, and after this we enter upon an era of rising prices in India. This may be regarded as having continued right up to 1920, except for the brief interval 1893-99, when

* For a study of the general course of prices from 1825 to 1907, see G. V. Joshi : *Writings and Speeches*. pp. 596-600 and from 1861-1893 Vakil and Muranjan op. cit. pp. 311-321.

† See Irving Fisher: *Purchasing Power of Money*, p. 142.

prices went down somewhat owing to the relative contraction of circulation in India after the closing of the mints to the free coinage of silver, though the effect of this factor was a little obscured by the famines during this period. The rise in prices was the outcome mainly of the depreciation of silver and the heavy rupee coinage between 1881-92. We have already described the causes of the depreciation of silver and explained how its demonetisation by Germany and other European countries led to a heavy inflow of silver into India whose mints were yet open to its free coinage.

§ 4. The Prices Enquiry Committee (1890-1912) :—The period covered by the Prices Enquiry Committee extended, as mentioned above, from 1890 to 1912, and the five years 1890-94 were taken as the base for comparing the price statistics relating to the later years. The base period was comparatively normal and free from the violent fluctuations witnessed subsequently as the result of the two severe famines at the close of the century.

‡ Index Numbers for India of the general average of Rupee Prices and Gold Prices for the years 1890-1912.

Year	Rupee Prices	Gold Prices	Year	Rupee Prices	Gold Prices
1890	97	113	1902	111	115
1891	98	106	1903	107	111
1892	103	100	1904	106	110
1893	102	96	1905	116	120
1894	100	85	1906	129	134
1895	101	89	1907	133	138
*1896	106	99	1908	143	147
*1897	121	120	1909	133	138
1898	106	109	1910	132	137
1899	104	108	1911	134	139
*1900	122	126	1912	141	147
1901	116	120			

‡ K. L. Datta's Prices Enquiry Report, p. 29.

* Famine years.

Until 1898, when the gold value of the rupee attained stability at 1 s. 4d., the Rupee and the Gold Index Numbers differ. Between 1890-94, the gold price of silver declined steadily. While the rupee prices fluctuated within moderate limits, gold prices of commodities fell in those years steadily from a level of 113 to 85. The steady fall in the gold value of the rupee was accompanied by a steady decline in the general (gold) price level. Between 1895-97, when the exchange was rising rapidly, the rupee price level as compared with the average for the quinquennium 1890-94, was higher than the level of the gold prices. Since 1898, when the rupee became practically stable at 1 s. 4 d., the Index Numbers of gold and rupee prices moved, as might be expected, in the same direction, although the former were higher than the latter by 4 to 5 points.

Taking now the whole period 1890-1912, there was a general rise in prices throughout India, being specially marked since 1905. Taking quinquennial periods, the Index Numbers for all India showed an increase in rupee prices of 8 per cent in the quinquennium 1895-99; 12 per cent in the quinquennium 1900-04; 31 per cent in 1905-09; 32 per cent in 1910; 34 per cent in 1911; 41 per cent in 1912, in comparison with the basic period 1890-94: or expressed in gold prices, a rise of 5 per cent in 1895-99; 16 per cent. in 1900-04; 35 per cent in 1905-09; 37 per cent in 1910; 39 per cent in 1911 and 47 per cent in 1912.† The rise in prices was specially marked in the case of hides and skins, food grains-pulses and cereals,-building materials, and oil-seeds, all of which rose 40 per cent or more above the level of the basic period. Cotton and jute rose about 33 and 31 per cent respectively, while other articles of food, metals, and other raw and manufactured articles rose by about 25 per cent. There was a moderate increase in country sugar; but on the other hand, there was an appreciable decrease in the prices of tea and coffee, imported sugar, dyeing and tanning materials, especially indigo, coal, and shellac, as also a slight fall in the prices of other textiles.

The extent of the rise in prices was not the same all over

† K. L. Datta, *op. cit.*, p. 46.

India, being greatest in famine areas such as Bundelkhand, Berar, Sind, Agra Provinces (North and West), Punjab East, Punjab West, the Deccan, and South Madras. The rise was comparatively small in Assam which is practically free from famine. The rise at the ports like Bombay, Calcutta, Madras, Rangoon, etc., was less than in most of the upland circles, though it should be noted that prices at the ports had been generally higher in the earlier years than in the upland circles. This phenomenon of a smaller rise in prices at the ports was due to the fact that they were less susceptible to fluctuations as they drew their supplies from a wider area. Also in the earlier years the prices at the ports had been generally higher so that an equal rise in prices would show a lower percentage of rise than in the upland circles.

While, however, there were striking disparities between the price levels in good and bad years, the inter-circle and inter-district variations showed a tendency to diminish with the linking up of markets by the railways. There was a tendency towards an equalisation of prices all over the country.

§ 5. Comparison of the Indian with the world price level.—In view of the general rise of prices throughout the world during the period of enquiry, the Committee instituted a comparison of the Indian price level with that of other countries. The table on the next page shows the range of increase in prices in different countries arranged in descending order. It gives the average prices during the quinquennium 1907-11 as compared with the averages of the basic period and of the quinquennium 1894-98, when the lowest level of prices was reached everywhere except in India.*

This table clearly shows that the rise in prices was greatest in India. The United States and Germany showed a considerable rise which may be attributed to their heavy protective tariffs and the influence of industrial and commercial combinations—factors which were practically non-existent in India.

* K. L. Datta, op. cit. p. 50.

Country		Compared with 1890-94	Compared with 1894-98
India	...	40	40
Belgium	...	25	26
Germany	...	24	38
U. S. A.	...	20	38
Canada	...	19	31
Italy	...	14	24
Australia	...	13	20
France	...	12	26
United kingdom	...	9	21
New Zealand	...	1	9

§ 6. Causes of the Rise of Prices (pre--War) in India: —The most controversial part of the Report of the Prices Enquiry Committee relates to the analysis of the causes of the specially high price level prevailing in India before the War. The Committee divide the causes into two classes, viz. (1) causes peculiar to India, and (2) causes not confined to India, i. e., world factors; though they recognise that the two sets of causes reacted on each other.

I. *Causes peculiar to India* :—According to the Committee the causes peculiar to India were (a) shortage in supply of agricultural products and raw materials; (b) increase in the demand for these commodities; (c) development of railways and other communications in India and the lowering of the direct and indirect costs of transport in India itself and between Indian ports and foreign countries; (d) improvement in the general monetary and banking facilities and increase of credit; (e) A Increase in the volume of the circulating medium etc.

II. *World factors* :—(a) The world factors were shortage in the supply of and increase in the demand for staple commodities in the world's markets; (b) the increased gold supply from the world's mines; (c) the development of credit; (d) destructive wars and increase of standing armies and navies in most of the West-

ern countries and U. S. A. diverting capital and labour into unproductive channels and causing an increased demand for many classes of commodities. India was switched on to the currency gauge of the rest of the world owing to her abandonment of the silver standard in 1893 and no doubt she shared in the price fluctuations in the rest of the world due to these causes. What we want to know, however, is why the price level rose higher in India than in other countries.

§ 7. Examination of the alleged causes peculiar to India:— Taking the Prices Enquiry Committee's Report as the basis for discussion we shall now examine some of the causes commonly advanced in explanation of the rise in prices in India. ¶

The Report puts down the phenomenon largely to the shortage in supply particularly of food grains owing to (i) the growth of cultivation not keeping pace with the growth of population; (ii) unseasonable rainfall; (iii) the substitution of non-food for food crops; § (iv) the inferiority of the new lands taken up for cultivation etc. The following table compares the growth of population with that of production of food grains and the extension of cultivation:—

	Average of the quinquennium.					
	1890-91 to 1894-95	1895-96 to 1899-00	1900-01 to 1904-05	1905-06 to 1909-10	1910 -11	1911 -12
Population	100	101.6	103.7	105.7	107.8	108.4
Total area under cultivation	100	98	103	105	108	106
Area under food grains	100	96	101	102	106	103
Production of food grains	100	98	105	99	113	109

¶ See Chabiani : op. cit. pp. 144-154.

§ Already discussed in Vol. I, see Chap. VI.

Mr. Datta concluded from this table that population had increased by a larger percentage during the period under enquiry than either the total area under cultivation, the area under food grains or the total production of food grains. During the same period also there was an increase in the external demand for Indian food grains. The increase in the internal demand was attributed by Mr. Datta to a rise in the standard of living of large sections of the people, particularly those engaged in the cultivation of jute, cotton, oilseeds and wheat. We have already noticed* that the Government of India did not accept this conclusion on the ground that Mr. Datt's data were largely conjectural and uncertain, and argued that the area under cultivation generally and that under food crops in particular had kept pace with the growth of the population and that there was an improvement in the outturn owing to the extension of irrigation.† We may remark here that, even although the area under cultivation may have kept pace with the growth of the population, this does not necessarily prove that there could be no rise in the prices of foodstuffs. Because the lands that were newly brought under cultivation were presumably inferior to those already under cultivation and consequently it would not be worth while cultivating them unless the prices were higher. The Government of India, however, were on firmer ground when they argued that there was an improved outturn from land owing to the growth of irrigational facilities.

The substitution of non-food crops for food crops which was alleged by the Committee as one of the causes of the increase in the prices of food stuffs had not in reality occurred to such an extent as to produce an appreciable effect on food prices. In any case, if there was a real shortage of food crops the food prices alone would have been affected, whereas the phenomenon to be explained is the rise in general prices which required some cause or causes also general in scope. Mr. Datta's whole treatment is vitiated by his failure to distinguish clearly

* See p. 90. Vol. I.

† See Resolution of the Government of India on the Prices Enquiry Committee's Report (paras 13-18).

between relative and general causes. Also he strays into the path of error by arguing as if the level of prices depended not on the relation between the volume of goods and that of the circulating media but on the former and the size of the population. † A general increase in the prosperity of all sections of the people which Mr. Datta regards as having been responsible for an increase in demand, appears to be *prima facie* improbable under the circumstances supposed. If the supply of food failed to increase in proportion to the population, this must mean widespread distress in a country like India which does not import foodstuffs from abroad except to a negligible extent, and in which agriculture is practically the only occupation of the people. If there was a universal increase in the standard of comfort this would have caused an all-round increase in productive efficiency, which by itself, unless it was accompanied by a corresponding increase in currency, ought to have occasioned a fall and not a rise of prices.

The development of communications would, on the one hand, tend to raise prices by increasing the rapidity of the circulation of money even assuming that there was no increase in the quantity of money, and on the other hand, it would tend to depress prices by increasing the volume of transactions. There is no evidence that the latter tendency was such as to overbear the former. The chief influence of communications, it must be remembered, is to make prices uniform so that they would be higher than before in some places and lower than before in others. But what we are seeking an explanation for is a universal rise everywhere. Mr. Datta isolates the influence of credit from that of metallic currency. He does not admit that the volume of metallic currency had increased more than the volume of business, but he thinks that there was a considerable growth of credit in India during the period under enquiry. As we shall show presently his former assertion was incorrect. And as regards the latter there was no such development in banking and credit as would have been necessary to produce the actual rise in prices.

† See Chabani op. cit. p 146.

As to the export of food stuffs producing a rise in prices in India, the following considerations must be borne in mind. In the first place, the proportion of exports to total trade never exceeded 7 per cent during the period in question and therefore their effect could not have been very great. Moreover, prices were actually lowest in years when the exports were highest. In fact, it was the prevalent low level of prices which was the cause of the increase in exports. Again, wheat (the principal article of food exported) constituted only 10 per cent of the total food produce in India, and the influence of the export of a part of this 10 per cent on the level of prices of food stuffs in general cannot be regarded as anything but negligible.

Other alleged causes are rise in wages, the import of capital into India and the influence of dealers' monopolies. As regards the first, it was in the first place a relative cause because there was no evidence whatsoever that there was a universal rise in wages in the agricultural and manufacturing industries. In the second place, it is well known that prices rise first and then wages. As regards the import of foreign capital this is an inadequate cause because in some years the interest paid by India balanced the capital sent to India. Similarly, with reference to the last of the causes mentioned, viz., dealers' monopolies it is hardly necessary to advance formal proofs that this cause was at best relative and in any case not adequate.

§ 7, Currency inflation the real cause:—By a process of elimination we arrive at the conclusion that the inflation of currency—which in India could only mean metallic currency owing to the inconsiderable development of credit—was the main cause of the rise in prices. The rupee being no more than a note printed on silver and being inconvertible into gold, it was almost as easy to issue it to excess as inconvertible paper notes. Its supply depended wholly on the discretion of Government who had the monopoly of its issue. We need not go to the length of suggesting that excessively heavy coinage was undertaken by Government deliberately in order to make profits. What is contended is that Government often wrongly though honestly supposed that more rupees were necessary, when in

fact they were not wanted, and straightaway proceeded to coin them. That on occasions excessive coinage did take place in this manner has been freely recognised even by Mr. J.M. Keynes, one of the warmest admirers of the Gold Exchange Standard in India, as seen from the following passage which occurs in his book *Indian Currency and Finance* (p. 134). "The coinage policy of the Government of India from 1905 to 1907 suggests one obvious reflection. A succession of years, in which there is a heavy demand for currency, makes it less likely that the demand will persist in the year following. The effects of heavy coinage are cumulative. The Indian authorities do not seem to have understood this. They were, to all appearances, influenced by the crude inductive argument that, because there was a heavy demand in 1905-6, it was likely that there would be an equally heavy demand in 1906-07; and, when there actually was a heavy demand in 1906-07, that this made it yet more likely that there would be a heavy demand in 1907-08. They framed their policy, that is to say, as though a community consumed currency with the same steady appetite with which some communities consume beer."

The view that heavy coinage was mainly responsible for the rise in prices was voiced in the Imperial Legislative Council by the late Mr. Gokhale in 1908* in the following words. "It seems to me, my Lord, that the phenomenally heavy coinage of new rupees during the last few years has something to do with this general rise in prices.....The stock of rupees in existence in India before 1898 was estimated by Mr. Harrison, the expert, at 130 crores. During the last ten years the Government has made a net addition to this stock of over 100 crores. It seems to me that such a sudden inflation of the country's currency is bound to result in a general rise in prices.....What is probably happening is this. The rupees issued by the Government in response to the demands of trade go into the interior and spread themselves among those from whom purchases are made. But, owing to various circumstances, they do not flow back quickly to centres of trade, or to banks, and these new rupees have to be obtained for transactions for

* Speeches of G. K. Gokhale, pp. 112-113.

which the old rupees might have sufficed. Meanwhile, the melting of rupees having ceased, (as a result of the token character of the rupee since the closing of the mints in 1893 and its artificial higher exchange value) every issue becomes a net addition to the volume of currency. If this analysis of the situation is correct, it suggests a grave problem, for it seems that prices will tend to rise still further. ”

Mr. Datta argues that the redundancy of rupees could not be considered to have taken place as the volume of business increased more than the volume of metallic currency. But if the expansion of business was more rapid it is difficult to see why prices should have risen at all. Again, in measuring the expansion of the volume of business, Mr. Datta is guilty of a serious error in that, instead of taking the physical quantities of goods handled in the way of trade, he takes their values in terms of money (inflated currency), thus showing an unduly high percentage of increase. While thus overstating the expansion in the volume of transactions, Mr. Datta understates the additions to the currency by failing to take into account the sovereigns and half-sovereigns and the small silver coins in circulation.*

The results of the enquiry by Professors Vakil and Muranjan bearing on this subject are set out below.

Period 1899-1913.

1899-1913 Rise in currency circulation	1899-1913 Rise in prices	1899-03 to 1901-13 Growth of goods
98.8 per cent	58.4 per cent	42.6 per cent

From these figures the authors conclude that, assuming world prices rose by approximately 25 per cent during this period, at least a quarter of the total addition to the currency between 1899-1913 must be held to be inflationary in character. ‡

* See Chablani : op. cit. p. 146.

‡ *Currency and Price in India*, p. 333.

There is a striking parallelism between the general index number of prices and the estimated total of the currency for each of the years between 1903 and 1907, as seen in the following table:—

Year	General in- dex nos. of prices	Estimated total of currency on the 1st of April of each year	Year	General in- dex nos. of prices	Estimated total of currency on the 1st of April of each year.
1903	100	100	1906	131	127
1904	102	110	1907	140	136 (April 1)
1905	112	115			143 (Dec. 1)

This shows clearly that the two were connected as cause and effect. Mr. Datta, however, objects to this conclusion and suggests that the parallelism is purely accidental. He urges that the average net coinage was much less during the period (1892-93)–(1911-12) than during (1874-75)–(1892-93). But he forgets that during the first period much of the coin was melted and there was scarcely any addition to the currency from year to year, whereas during the second period melting ceased as one of the results of the closing of the Mints, so that every rupee coined was a positive addition to the existing stock. It must also be remembered that, before 1893, the value of the rupee depended on the value of silver and the latter depended on the changes in the supply of silver (assuming demand to remain constant). The annual additions to the supply by imports of silver were so small relatively to the total stock of silver in the country, that it could not cause any noticeable alteration in the value of the metal and therefore in the value of the rupee. But after 1893 the main factor determining the value of the rupee was the quantity of rupee coins (and not silver) in existence at any given time, and since the annual coinage added considerably to the number of rupees already in circulation, the effect on rupee prices was pronounced.*

* See Chabiani : op. cit. pp. 151-52

Mr. Datta argues that there could not have been any redundancy of rupees for any length of time during the period in question, because if it had existed it would have caused an export of gold and there would have been a continued fall in exchange; and that as this effect was not visible the theory of inflation falls to the ground. Mr. Datta, however, wrongly imagines that the suggested effect on exchange was related to high prices, only if brought about by inflation of currency. As a matter of fact, his objection, in so far as it is valid at all, is valid not merely against this or that particular alleged cause of the rise in prices but against the phenomenon of higher prices in India than world prices. The fact of the higher prices, however, must be taken as established beyond controversy, and Mr. Datta himself not only admits it but it forms the whole basis of his own inquiry. The question why in spite of the disparity between the internal and external value of the rupee the exchange remained steady is not relevant to a discussion concerned with the ascertainment of the causes of the higher level of prices in India than elsewhere.*

§ 8. War-time prices:—The pre-war tendency of prices to rise which we have discussed so far manifested itself in an unprecedented degree during the years 1914-1920, especially during the latter part of this period owing to conditions created by the War. The rise in prices was, however, smaller in India than in some other countries, especially in those that were directly engaged in the War as seen from the annexed table (See next page).

During the period 1914-20, prices rose enormously in practically all countries and especially rapidly during the latter part of the period reaching their maximum in 1920. Prices in India did not rise as fast as, for example, in the United Kingdom and France. Let us now discuss the causes of the rise of prices in India during these years and try to explain why the rise was not as high as in some other countries.

* For an interesting but not wholly convincing explanation of the steadiness of exchange, See Vakil and Muranjan: op. cit. pp. 328-329 and p. 334.

Index Numbers of prices in India and some foreign countries.

Year	*India	U. K.	U.S.A.	France	Japan	Canada
1913		100	100	100	100	100
1914	100	100	98	102	96	102
1915	112	127	101	140	97	110
1916	128	160	127	188	117	132
1917	145	206	177	262	149	179
1918	178	226	194	339	196	199
1919	196	242	206	356	236	209
1920	201	295	226	509	259	244
1921	178	182	147	345	200	172
1922	176	159	149	327	196	152
1923	172	159	154	419	199	153
1924	173	166	150	489	207	155
1925	159	159	159	550	202	160
1926	148	148	151	703	179	156
1927(Jan)	146	144	147	622	170	151
1928(Sep)	148	139(Aug)		624(Jul.)	169(June)	150(July)

During the war period, the prices of practically all commodities in India, including the necessities of life, showed a very steep rise. The following table † shows the price changes affecting certain commodities between the years 1913-20.

1913=100

	1913			1920			Percentage change
	Rs.	as.	p.	Rs.	as.	p.	
Rice Per Maund	5	3	9	8	6	0	161
Wheat do.	3	11	6	7	0	0	188
Jowar do.	3	0	0	5	8	0	183
Salt do.	0	8	7½	1	8	2	280
Cotton cloth per piece	5	4	0	14	2	0	269

* The index numbers for India are those of wholesale prices at Calcutta with July 1914 = 100 (the index number for 1928 Sept. is for Bombay.) See the Review of Trade for India 1926-27, and Labour Gazette, Bombay, Oct 1928.

† Stanley Jevons : *Money, Banking and Exchange*, p. 261.

By 1919, the prices of food grains had risen on an average by 93 per cent since the commencement of the War, while the increase in piecegoods was just under 190 per cent for imported goods and just over 60 per cent for Indian made goods. We have already observed that the prices of the imported goods such as cotton piecegoods, steel and iron, sugar, dye-stuffs, etc. in general rose much more than those of the exported goods and also explained the causes of this disparity.* The remarkable rise of prices in India was partly due to world factors and partly to factors peculiar to India. The diversion on the part of the principal nations of Europe of their energies to the work of destruction instead of production had naturally led to a world shortage of the necessities of life. The shortage of production as well as the intense competitive demand of the belligerent countries for commodities of all kinds together with the creation of a huge volume of credit and currency to finance the War were responsible for the phenomenal increase of prices. These world conditions were bound, sooner or later, to react on India by increasing the demand for her products abroad as well as by adding to the cost of articles she imported. The restrictions imposed on exports partly by the shortage of tonnage and partly by Government control seemed to check the rise in prices in India to some extent. Nevertheless many of the causes in operation in the world at large could not altogether be prevented from coming into play in India as well.

§ 9. Inflation of currency:—We have already noticed that for some time after the outbreak of the War, the balance of trade remained strongly in favour of India. At the same time there was a serious reduction in the imports of treasure thus throwing upon the Government the whole of the responsibility of financing the export trade by issuing a large volume of additional currency in the form of rupees as well as currency notes. The process of inflation was also helped by the methods of war finance adopted by Government. In order to meet the heavy war expenditure they furnished themselves with the means of payment partly by raising taxation and loans representing the

* See chapter VII, Trade of India.

real savings of the community and partly by the artificial creation of purchasing power. Government possessing, as it did the absolute monopoly of note issue, was able directly to provide itself with the means of payment by watering the paper currency. The War loans of Government also inevitably led to inflation. Only a portion of these loans came out the real savings of the people. The remainder took the form of bank credits or the creation of deposits subject to cheques which the banks opened in favour of Government on their own account or on behalf of their customers who wished to invest in the war loans.* The short-term Treasury Bills which were issued by the Government of India for meeting the successive budget deficits was another source of inflation as the banks lent freely against their security and that of the War Bonds. Thus there was a very large increase in the bank deposits or credits as well as in their velocity as shown by the bank clearings,† which supplied so much more buying power and contributed to the rise of the prices.§ The following table shows the growth of circulation from 1914 to 1919.¶

(In crores of rupees).

	1914	1915	1916	1917	1918	1919
Rupee circulation (active)	187	204	212	227	219	228
Note circulation (gross)	66	62	68	86	100	153
" (Net)	59	56	64	82	98	150
" (Active)	50	44	53	67	84	134
Total Rupee and note circulation (Active)	237	248	265	294	303	362
Cheque currency (Bank clearings.)	538	563	809	901	1396	...
Total Rupee, note and Cheque currency	775	811	1074	1195	1699	...

* Panandikar pp. 317-318.

† See also Chapter on Banking.

§ See Findlay Shirras pp. 410-411.

¶ Findlay Shirras, op cit. p. 232.

The rise of prices in India was not so high as in other countries because Indian prices were not subjected to the same strain as elsewhere. The extent of the inflation of paper money, for example, was far less in India than in some of the foreign countries.

It should also be noted that owing to the excessive inflation of currency, its rapidity of circulation increased proceeding from and reflecting a diminished level of public confidence as in Germany and Russia though to a very much smaller extent in India.*

As a further contributory cause of the rise of prices must be noted the relatively small growth in the volume of business which lagged considerably behind the total expansion of currency of all kinds. According to Prof. Findlay Shirras, taking the average of the figures for 1911-1913 as 100, the whole index number for the total rupee note and cheque currency (without taking the rapidity circulation into account) increased from 95 in 1914 to 201 in 1918, whereas during the same period the index number for the growth of business increased from 113 to 126.* Under these circumstances a sharp rise in prices was inevitable.

There were other causes which aggravated the rise. Reference has already been made to the breakdown of the railway system and the shortage of rolling stock during the war years. This led to difficulties in the distribution of goods and thus accentuated the effect of local scarcity incidentally creating golden opportunities for the profiteer. Moreover, during the year 1918-19 there was a widespread failure of the monsoon in India, which caused a serious shortage of foodstuffs. There was again a failure of rains during the latter part of 1920 with similar consequences.

§ 10. Post-War trend of prices:—Prices in India having reached their maximum in 1920 began to decline from 1921, and for some time the process was more rapid in the United Kingdom than in India. As we have already seen, this endangered the policy of Government to stabilise the rupee at 2s. gold.

§ D. T. Jack: *Restoration of European Curreneies*. p. 3.

*Findlay Shirras, *op. cit.* p. 232.

The sale of the Reverse Councils in 1920 and the consequent deflation of currency led to a fall of prices. Also as a result of the adverse balance of trade in 1920-21 and 1921-22 there was an actual export of gold from India. Lastly, there was the influence of world forces on Indian prices explaining the striking parallel downward movement of prices in India, the United States and the United Kingdom in recent years.

The influence of the 1s. 6d. ratio in depressing the Indian prices has already been exhaustively dealt with and we need not say anything further here on that score. The decline in prices may in general be attributed to the gradual restoration of normal conditions in most countries in respect of monetary circulation and production of commodities and commerce. There is a general improvement noticeable in the purchasing power of money, though prices in India, United Kingdom and the United States are still appreciably above the pre-War level, showing that the process of restoration is not yet complete, and it may be added that perhaps it will never be complete if by completion we understand a return to the pre-War level of prices. Very probably the rise in the price level throughout the world is a permanent legacy left by the War.

§ 11. Effects of high prices :—The Prices Enquiry Committee held that the high prices in India before the War benefited the country as a whole. This view was then endorsed by Government in their Resolution on the Report of the Committee (1914). The Committee argued that India being a debtor country with large foreign obligations which she meets by the export of part of her produce, she benefits when the prices of such produce rise because then she is able to discharge her foreign obligations by the export of a smaller volume of commodities. But as against the high prices of exports we must set the increased prices of imports and the higher cost of production. In any case it is difficult to believe that a higher range of prices, especially when it is due to an inflation of currency, is by itself capable of conferring any permanent advantages on the country as a whole sufficient to offset its well-known disadvantages. The Hon'ble Mr. G. V. Joshi after all expressed what is the sound view in this matter when he observed that, "a real increase of wealth and prosperity comes to

nations as it does to individuals, not from any reckless piling up of coined rupees nor again from any rise of prices.....which... is in India almost invariably associated with crop failures and famine conditions, but only from an increase in industrial activity, energy and efficiency on the one side, and on the other, from increased productive employment of capital.”*

Violent price fluctuations are without question highly injurious to society. The incidence of the burdens they create and the benefits they confer is unequal and does not answer the ends of social justice. Monetary instability causes “a redistribution of the favours of fortune so as to frustrate design and disappoint expectation,” and it destroys the atmosphere of security which is essential for the confident pursuit of economic activities. On these general grounds we must regard with suspicion any attempts to prove that large and sudden price fluctuations either in the one direction or the other are beneficial to the country as a whole.

With reference to the temporary advantages and disadvantages accruing from price fluctuations to particular sections of the community one part of the problem has already been dealt with in connection with the ratio controversy. We had then occasion to describe how the different classes were affected by falling prices, and inferentially we may be said to have described the effects on them of a rise in prices also. For, all that is necessary for us now to do is to reverse the propositions laid down in connection with the falling prices in order to get an idea of the adventitious gains and losses arising from rising prices.

However, it may be instructive to set forth more explicitly the consequences of price fluctuations in recent times in India and examine how different sections of the population have fared under them.

§ 12. Effect on agriculturists :—It is often tacitly assumed or openly declared that landholders and the village people in general must necessarily benefit by high prices for agricultural produce. In India, however, we have already seen that the

* See G. V. Joshi's Speeches and Writings, p. 610.

gains of the agriculturists are intercepted to a very large extent by the numerous class of middlemen who intervene between the consumer and the agriculturist, and the high prices consequently do not result in any appreciable advance in the economic condition of the agriculturist. We must also take into account the fact that, while cultivators of their own land and of lands rented on long leases depending on their own labour and having a surplus to sell, stand to gain by high prices, this does not hold good of those who have to make rent payments in kind or who have received advances repayable in grain, or again those who hold short-term leases of land or have to employ hired labour. Moreover, both classes of cultivators have to reckon with increased prices of commodities like cloth, oil and other prime and conventional necessities of life.

§ 13. Rural Labourers:—It is almost axiomatic that wage movements lag behind price changes, so that when prices rise there is a shorter or longer period of hardship which the wage-earners must generally go through. In this connection it is necessary to bear in mind that many petty cultivators in India are also wage-earners. According to Mr. Datta, however, the wages of rural labour—agricultural labourers and village artisans—rose faster before the War, than the retail prices, and the rise was the greatest in rural areas where the real wages of these classes showed an increase of 38 per cent. Similarly, during the War and post-War period there has been apparently a progressive adjustment of rural wages to prices established after an interval of considerable suffering during the period of non-adjustment. “Throughout the period under review (1921-22) unskilled agricultural labourers commanded such high wages that in certain parts of India cultivators found a more certain and profitable means of livelihood than agricultural work.” The fall in prices since 1921 has further secured ¶ to the rural labourer some increase of real wages, though it must be admitted that even so his condition remains sufficiently deplorable.

* Report p 169.

¶ India in 1921-22 : p. 103.

As illustrating these remarks the subjoined table* showing the course of wages in the Bombay Presidency is of interest:—

(A) Wages in urban areas (District headquarters towns.)

Presidency Average (including Sind)	Average daily wages per head in			Increase per cent in 1926 over 1913.
	1900	1913	1926	
Field Labourers	Rs. 0 as. 3 ps. 0	Rs. 0 as. 4 ps. 9	Rs. 0 as. 10 ps. 6	121
Ordinary Labourers.	0 4 3	0 6 3	0 12 9	104
Skilled Labourers	0 10 9	0 13 9	1 13 9	116

(B) Wages in rural areas.

Field Labourers	0 2 6	0 4 3	0 8 3	98
Ordinary „	0 3 0	0 5 3	0 9 6	81
Skilled Labourers	0 9 0	0 11 9	1 9 3	115

§ 14. Effects of high prices on rural prosperity in general:—
Dr. Mann's conclusions with regard to the effect of high prices on rural prosperity in general are so instructive that we make no apology for reproducing his summary.

I (a) A 50 per cent rise in prices without a corresponding increase in wages makes for the advantage of those who have sufficient land which they work with their labour to maintain themselves in a sound position. (b) The man who benefits most is the non-cultivating proprietor who works his land by labourers. (c) Where there is a combined dependence upon the land worked by a family and upon income derived from the family's labour the final position depends solely on the proportion between

* See Report on 'Enquiry into Agricultural Wages in the Bombay Presidency' (1924) and Bombay in 1926-27.

the income from self-worked land and that from labour. (d) But the general effect on the village population is disastrous; and the annual deficit of expenses over earnings among the families belonging to the village increases enormously.

II. If prices as well as wages rise, say, by 50 per cent, the people belonging to class (a) are again much better off. (b) The non-cultivating proprietor is not appreciably affected except in so far as he has large debts. The position of the people of class (c) is still improved and the improvement is slightly greater than the rise in prices; (d) the general effect on the village population is to lower their economic position.

III. With a rise of prices, whether wages increase or no, two general results seem to ensue. (1) The gulf between the solvent and insolvent of the villagers tends to widen, the vast majority of the people previously solvent becoming more so, while the position of the insolvents deteriorates. (2) On the other hand, since the rate of interest, which is always high in India, does not increase with the rise in prices, those who have incurred large debts previously suffer less in proportion than the others. On the whole, it may be said that a rise in prices tends to emphasise economic differences throughout the rural population in India, those who are well-to-do becoming more well-to-do and those who are poor becoming poorer.

§ 15. Effects on rent receivers :—Regarding the effects of a rise in prices on cash rents, a distinction is necessary between protected or privileged, and unprotected classes of tenants. In the former case, illustrated by the class of occupany tenants, rents would naturally show a comparatively small rise; while in the second case there have been large increases, for example, in Bombay, where rents have soared to great heights, particularly in the cotton tracts. It is thus clear that the class of the rent-receiving landlords has been adversely affected where their lands have been let out on a more or less permanent tenure. §

§ It may be noticed that in recent years there has been an attempt on the part of the labouring and tenant classes to secure for themselves the advantages of collective bargaining by the formation of Tenant Unions and Kisan Sabhas. See India in 1921-22, p. 199.

§ 16. Effects on Industry: (i) *Handicrafts*:—We have already drawn attention to the condition of economic stagnation of persons engaged in indigenous handicrafts owing to the competition of machine-made goods. The rise in prices has, if anything, increased the severity of this competition and made the position of the handicraftsmen even weaker than before.

(ii) *Capitalist manufacturers*:—The case of capitalist manufacturers is more complicated, for, generally speaking, the rise in prices is not immediately followed by a proportionate rise in all the costs of products including wages. Therefore, *prima facie*, this class should benefit at least in the beginning. But, as will be shown below, the wages of the operatives in the manufacturing industries have in most cases exceeded the rise in prices. The fall in prices since 1920 has further increased the real wages of factory labour, and since no proportionate increase in efficiency, though it may be expected to come in the long run, is as yet in evidence, the manufacturers have on the whole suffered on the score of wages. The higher level of prices in India and the lower level of prices abroad together with the fixity of exchange have also rendered foreign competition keener in the Indian market.* The present position of the manufacturers therefore is on the whole most unenviable. The rise in prices during the War and the early post-War period no doubt brought them immense profits. But these profits were mostly dissipated in the distribution of recklessly high dividends, instead of being utilised for strengthening the reserves. "Full steam ahead and damn the consequences" seemed to be the motto of the mill-owners and they are now paying the penalty for this policy. The difficulties of the present period of depression could not indeed have been avoided altogether by any amount of foresight, but the lack of foresight has certainly added to them to an appreciable extent.

§ 17. Labour in cities and towns:—In the pre-War period, as Mr. K. L. Datta shows, the nominal and real wages of the different classes of labourers rose, though the rise in real wages

* Wadia and Joshi : *Money and Money Market*, p. 257.

was not so high as in the rural areas, being 33 per cent in the urban areas and 28 per cent in the cities.* We have already traced the course of wages in the case of industrial labour during and after the War (with special reference to conditions in Bombay). The rapid rise of prices between 1917-20 led to a perfect epidemic of strikes, and in some cases there were even bread riots and looting of bazars. Since 1921, however, there has been a definite improvement in the condition of industrial labour both by an increase of wages and a progressive fall in the cost of living.

§ 18. Effects on persons with fixed incomes:--The worst sufferers from high prices are persons with fixed money income, like pensioners, clerks and, in general, the lower grades of state and commercial employees, or those dependent on income from securities and shares, and professional men who live upon customary fees. These classes, collectively styled as the middle classes, suffered greatly during the period of high prices owing to their fixed money earnings and the heavy increase in the cost of food, clothing, lighting, house rents, and the wages of such labour as they happen to employ. Their social status debars them from undertaking work of certain kinds, while the market in which they themselves compete for employment is chronically overstocked. Nor have they yet learnt the value of organisation and collective bargaining.

The foregoing discussion brings out the uneven incidence of large and rapid price movements on the different strata of society and the importance of securing stability in the purchasing power of money.

* Domestic servants in towns and cities did not benefit to the same extent as the other classes of labourers from a rise in their wages. Nor was the rise in the real wages of all industrial labour as large as in the case of e. g. the Bombay factory labour. Nominal wages increased in all cases, but the rise was in some cases not even equal to the rise of prices, especially in the case of coolies in the tea gardens, brewing and sugar industries.

CHAPTER XI

BANKING AND CREDIT.

§ 1. Constituents of the Indian Money Market:—The Money Market and Banking System of India comprise the following principal constituents:—(1) The Imperial Bank (originally the Presidency Banks). (2) The Foreign Exchange Banks (mostly European or foreign); (3) The numerous and heterogeneous group of Indian bankers and brokers called by different names such as Shroffs, Multanis, Banias, Marwaris, Sawkars, Mahajans, and Chetties, whose operations are almost entirely confined to the interior of India. (4) The Indian Joint-stock Banks on European lines.

In addition to these four main types, there are the Postal Savings Banks, Co-operative Banks, and Industrial Banks, to which may be added the Land Mortgage Banks which have recently come into existence.

HISTORY OF INDIAN BANKING.

§ 2. Indigenous Banking:—Indian banking is as ancient as Indian commerce. Perhaps India knew more about banking and knew it earlier than any other country in the world.* The Arthashastra of Chanakya (about 300 B.C.)† describes powerful guilds of merchant bankers who received deposits, advanced loans, and in short, carried on functions in many ways comparable to those of modern banks. Meadows Taylor in his *Student's Manual of the History of India* gives a flattering description of ancient Indian Banking in the following words: "The laws of Menoo disclose how thoroughly the science of banking was known 3000 years ago.

* "From times immemorial the banker has been an indispensable pillar of Indian society."....."There is plenty of evidence to show that even prior to the advent of occidental ideas India was no stranger to the conception of banking." M. L. Tannan; *Banking Law and Practice in India*, p. 2.

† Translated by Shamasastri, Mysore.

Then bankers understood and followed the fluctuations of money value: they kept account books, day-books and ledgers by single and double entry. They charged interest simple and compound, they made insurances by sea and land, they granted bills of exchange, and in short they followed the practices of modern times which are little changed from ancient rules."

The Mahomedan invasions of India initiated a period of disturbance and insecurity which were fatal to these old banking institutions. It was no longer safe for people to entrust their savings to them, which began consequently to be secreted in hoards. Individual bankers, however, continued to prosper and they usually combined commerce with banking. They advanced loans to the State, and many influential bankers' families were attached to one or other of the native courts. "No royal court was complete without a State Banker, who was often invested with the powers of a minister." The history of the house of Jagat Seth, hereditary bankers of the Nabobs of Bengal, shows the important part played by these bankers in the politics of the country.*

Even the East India Company had to rely on the Indian bankers for loans and remittances, and they continued to wield a dominant influence as state financiers till the advent of the European Agency Houses.

Even now the Indian banking system plays a very important part in the monetary organisation of the country. The Indian banker is to be found in every village, town and city in the country. "The type ranges from the small village capitalist, the wealthy well-established private partnership, generally a family partnership, of merchant bankers which has agencies in and outside India. A special type is that of the Chetty community in Madras, where there exists something approaching to joint responsibility of the Community as a whole." † The Natukottai Chetties of the Madura District of Madras are especially famous as traders and bankers and their operations are almost

* See H. Sinha: *Early European Banking in India*, pp. 1-2.

† Gubbay: *Indigenous Banking in India*, pp. 11-12.

world-wide in their scope.* The banking business carried on by the Indian Shroffs and money-lenders must be enormous in the aggregate. It is conjectured that, taking into account only the short-term advances to trade and commerce and the long-term advances made by money-lenders against mortgages, it amounts probably to more than 100 crores of rupees.† The general standard of business morality among the Indian bankers has been universally recognised to be very high. Indigenous Indian banking is not organised on the joint-stock basis. Generally also there is comparatively little capital from deposits. There is no share capital and the liability is single or, in the case of a partnership, joint, and it is unlimited. In principle there is no difference between the transactions of the Indian banking firm or shroff and those of any private banking firm in any other country, except that the former often combines trade with the business of finance§ and that the latter has developed a system of payments by cheques. The Indian shroffs, unlike the English bankers of the 18th century, never issued any notes payable on demand, although legal prohibition to issue notes did not exist for a long time. The great difference between modern banking on European lines and the indigenous banking system arises from the growth of joint-stock banks in modern times and the universal use of the cheque as a means of remittance through the mechanism of clearing houses. In times gone by, the principal business of the shroffs was to change money, a function which, as we have seen, was especially important when each petty state minted its own standard coin and the country was flooded with a large quantity of varied forms of metallic money. The Shroffs also gave letters of credit, dealt in Hundis, which are the indigenous analogue of cheques or

* For an interesting survey of indigenous banking as carried on by the Nattukottai Chetties See T. K. Doraswami's Paper on "Some Aspects of Indigenous Banking in the Madras Presidency," read before the Indian Economic Conference, Bombay, 1924.

† B. T. Thakur: *Organisation of Indian Banking*, p. 44.

§ It has been suggested that this combination of functions is one of the reasons why Indian Banking having arrived at a certain high state of development has not progressed further.

internal bills of exchange, and occasionally helped the state in financing great undertakings.

§3. Present position of indigenous banking:—Even at the present time the Shroff continues to play an important part in the financial system of the country as an indispensable link between the Indian money market and the vast trading community. He finances the agriculturist, the petty artisan and the small trader, assists in the movement of crops to consuming areas or to the ports and distributes all kinds of goods in the interior of the country. He sends his agents with specie by rail, when necessary, in the harvest season, or he buys bills on Government treasuries and when in need of funds discounts his bills with the Imperial Bank or other banks in the commercial towns.* The indigenous bankers are in some ways formidable competitors to the big joint-stock banks organised on modern lines. As they pay a higher rate of interest they are able to attract deposits more readily than the bigger banks. They also lend on personal security, and, in general terms, their requirements with regard to security are more easy to satisfy than in the case of banks. They are also at an advantage because under the present conditions the modern type of banks in India can never hope to get into sufficiently close touch with the affairs of the vast trading community all over the country to enable them to grant accommodation directly to more than a few of the bigger traders. The Indian bankers, therefore, are under existing circumstances, indispensable middlemen. The Babington Smith Committee describes the manner in which the indigenous financial agency has been made to fit in with the modern monetary organisation in the following words: "The people with whom the banks deal directly are for the most part large shroffs of good standing in the principal cities. These men operate with their own capital, and generally speaking, it is only when they have laid out all their available capital in purchasing the Hundis of other and usually smaller shroffs that they come to the Presidency Banks. The shroffs, whose Hundis the larger shroffs have purchased, have probably also similarly financed other and still smaller shroffs or Mahajans, and so on, until we

* See Shirras, *Indian Finance and Banking*, p. 241,

get down to the smallest flea of all, viz., the village bania or grain-dealer or goldsmith. For instance, shroff A at Amritsar may purchase a bill drawn by a larger shroff at Lahore, who sells it to the Presidency Bank, which sends it to their Bombay Agency for collection, or the bill may be a pure finance bill generally known as a hand bill as opposed to a 'trade' bill, drawn against produce."

The growth of modern banking has not affected the business of the shroff. On the other hand, he has good reason to welcome it as relieving him of much inconvenience, e. g., as regards sending specie and obtaining accommodation. He buys the Hundis drawn by the trading community, charging them a rate of discount above the bank rate, the difference constituting his profit. * Though some of the indigenous private banking firms are being converted into private banks conducted on modern lines and issuing cheques, most of them still follow their old traditional methods.

§ 4. Beginnings of modern banking.—The European system of banking was first introduced into India by the Agency Houses of Calcutta, who started a banking side as an aid to the conduct of their business. In their capacity as bankers, the Agency Houses did business with the merchant princes in India and with the planters, advancing loans on mortgages of ships, indigo factories etc. The European community in India and the English officers of the East India Company deposited their savings with them in preference to investment in public securities owing to the attractive rates of interest offered by the Agency Houses. The Agency Houses came to grief as a result of engaging in speculating transactions, and the commercial crises of 1829-32 put an end to them. The banks managed on European lines were thus not at first joint-stock banks, nor are they so exclusively at the present day. European firms like Messrs Cox and Grindlay, and navigation companies like the Peninsular and Oriental Company have a banking side to

* This rate of discount is as a rule 2 or 3 per cent above the Bank Rate in Calcutta, and about 1½ per cent in Bombay, where the competition amongst the shroffs is unusually keen.

their business. The first purely banking institution on European lines was the Bank of Hindostan established in Calcutta by Messrs Alexander and Co. The Bank disappeared in the crisis of 1829-32 when the firm of Messrs Alexander and Co. failed along with others. On their ruins arose the Union Bank, a joint-stock bank created by co-operation among all the leading Calcutta houses, but it also disappeared in 1848.

§ 5. The Presidency Banks:—The foreign trade of the country was comparatively small in the earlier part of the 19th century and the financing of the internal trade was looked after by the indigenous bankers already described. As trade gradually developed the need of banks of European type was experienced, added to which was the interest of the Company's Government in regard to its own banking business. Reliance on the Agency Houses or on the Indian bankers was being found so expensive and unsatisfactory that it sufficed to overcome the reluctance which the Company had displayed so far to promote the establishment of new banking institutions. Under these circumstances, the Bank of Bengal, the oldest and the most powerful of the Presidency Banks was established at Calcutta in 1806 by a Charter issued by the East India Company with a capital of 50 lacs 10 lacs being contributed by the East India Company. The first Bank of Bombay was established in 1840 with a capital of 52 lacs of rupees, 3 lacs of which were subscribed by Government. This Bank came to grief in 1868 as a result of its participation in the wild share speculation caused by the civil war and cotton famine in America. A second Bank of Bombay was established in the same year with Rs. one crore as capital. The Bank of Madras was started in 1843 with a capital of thirty lacs, three lacs being subscribed by the East India Company.

The establishment of the three Banks put an end to the possibility of the Bank of Bengal becoming a Bank for all India, an idea which had been in the air for some time.

From the very beginning, the Presidency Banks had a close connection with the Government of the country, which not only subscribed a part of the capital, but also had the right to

nominate some of their directors. Up to 1857 the office of the Secretary and Treasurer was usually held by a Civil Servant of the East India Company. In return, the Banks enjoyed some concessions, of which the monopoly of Government banking was the most important. The right of note issue had little practical value on account of several restrictions such as that the total liabilities on demand were not to exceed three times the cash reserves at first and four times afterwards. From 1839 onwards even the total amount up to which the notes could be issued was fixed. In 1862, as we have already seen, the right of note issue was taken away, Government having introduced their own paper currency. As a sort of compensation, the cash balances of the Government were placed with the Presidency Banks at the presidency towns.

By the Presidency Banks Act of 1876 Government withdrew their portion of the capital and relinquished the right of appointing Directors and Secretary and Treasurer. After this the Presidency Banks lost their official character but remained distinct from other banks, being governed by the special Act of 1876 and regarded both by the public and Government as the most important constituents of the banking system of the country and as an integral part of the Indian Treasury System. The bulk of their business was like that of any ordinary bank, viz., receipt of deposits and discounting. But they acted as bankers for Government to a limited extent. For instance, they managed the temporary public debt of the Government of India and enjoyed the privilege of using certain minimum Government balances. Although not State Banks, they always had some connection with the State, and under the special Act of 1876, Government was entitled to audit their accounts, to call for information and to make it obligatory on them to publish weekly statements of their accounts. This public control was intended to safeguard Government interests and ensure a development of banking on sound lines in the country.

§ 6. The Reserve Treasury System :—Between 1863 and 1876 the whole of the government balances at headquarters were kept with the Presidency Banks. But trouble having

been experienced in getting the funds back from the Banks of Bengal and Bombay, the Government of India established their own treasuries (Reserve Treasuries) in 1876 at Bombay, Calcutta and Madras. The Government balances henceforward were held largely in these three Reserve Treasuries, only small amounts-just enough for safety and day-to-day requirements-being held in the District and Taluka Treasuries. Under the new arrangements which came into operation in 1876 Government agreed to pay interest to the Banks on the difference between the actual deposits and the minima fixed, in case the former fell short of the latter, but they gave no undertaking to keep any balances whatsoever with the Banks. Actually the Banks always held cash balances generally in excess of the minima, though they were far from satisfied with this. A large amount of revenue flowed into Government Treasuries and remained locked up there especially at a time when it was badly wanted by the money market. India is an agricultural country with its busy and slack seasons varying to some extent in the different parts of the country. Broadly speaking, December to June is the busy season, and July to November is the slack season, except in the case of Calcutta where the busy season falls between July and October. The receipts of revenue are heaviest during the four months from January to April, so that the heavy revenue period synchronizes with the busy business season. Government have to maintain large working balances as the receipts of the revenue are very unevenly distributed throughout the year, whereas their expenditure proceeds at an even pace.* It was, however, generally felt that it was possible for Government to extend greater assistance to the money market without endangering their own safety.

Various proposals were made from time to time by the Presidency Banks and the Chambers of Commerce to the Government that loans should be issued to the public for short terms from the Reserve Treasuries through the Presidency Banks so as to avoid undue stringency in the money market. Government

* See Wattal : *The System of Financial Administration in British India*, pp. 200-202.

were unwilling to accept these proposals on the ground that under the peculiar circumstances of India they were subject to sudden calls and emergencies, and that, loans, besides being unsafe to Government, would also be undesirable for trade itself, which was likely to be led into dangerous commitments, if it came to regard capital supplied by Government and not representing the savings of the community as a resource on whose permanence reliance could be placed. Persistent representations, however, evoked a qualified response when the Government of India proposed to the Secretary of State in 1898 that it should be recognised as part of the business management of the Treasury Balances to lend money to the Presidency Banks at 1 per cent less than the declared minimum rate of interest during the months of January to May of each year, and the Secretary of State accepted the proposal subject to the condition that these loans should not be allowed to interfere with the Government disbursements in India and remittances to England and that they should be made at the current Bank Rate. These conditions being too rigid, loans from Government were rarely resorted to. The Chamberlain Commission, as an alternative to the partial or complete abolition of the Reserve Treasury System and the transfer of these funds to the Presidency Banks, proposed that these conditions should be relaxed and that loans should, in the first instance, be given to the Presidency Banks at 1 or 2 per cent below the Bank Rate. During the War, Government placed large funds much in excess of the minima, at the disposal of the Presidency Banks in order to facilitate the investment by the public in the War loans. The Reserve Treasury System is now abolished (since 1921), and the Government balances over and above those in the district and sub-treasuries are kept with the Imperial Bank at its head offices and its branches wherever it has got them.

§ 7. Business of Presidency Banks : Permissions and Prohibitions:—The Presidency Banks were permitted to do certain kinds of business and prohibited from doing certain other kinds. Briefly, (i) the Banks were excluded from dealing in foreign exchange (except as regards Ceylon in the case of the Bank of Madras); (ii) they were also prohibited from borrowing money

abroad; and lastly, (iii) there were certain restrictions as to the amount of the advances and the period for which they were made as well as the securities against which they could be made.

Turning to the business permitted to the Banks, they could receive deposits and invest in Government and other specified securities of public bodies and corporations. They were allowed to draw and discount bills of exchange payable in India. They could advance funds against accepted bills of exchange and promissory notes, accept securities for safe custody, and buy and sell gold and silver and manage Government loans at the Presidency towns and the debt business of certain municipalities. Some of these restrictions were due to the jealousy of the East India Company, which first imposed them, especially those in regard to the raising of funds in London. The exclusion from foreign exchange business was due the supposed uncertainties attendant on it. The Banks made several representations urging the relaxation of some of these restrictions, but without success. Similarly, as noted above, the establishment of the Reserve Treasury System prevented the Presidency Banks from using Government funds to finance trade in the busy season so as to introduce some measure of elasticity in the Indian money market.

§ 8. Progress and relative position of the Presidency Banks :— All these restrictions and handicaps, however, did not prevent the Presidency Banks from prospering greatly. The restrictive provisions, while they hampered an even more rapid development than was actually achieved, conduced to the stability and strength of the Banks. As we saw above, the Government always kept some balances with the Banks, which were usually in excess of the minima fixed, and the Banks also did some general banking business for the Government, wherever they had branches, for which they received some fixed remuneration. Further, the Banks undertook to provide special facilities for the encashment of the currency notes at their branches in order to popularise them. This association of the Banks with Government added greatly to their prestige and stood them in good stead since it attracted private deposits and banking business on profitable terms and helped them to

acquire and maintain a position of pre-eminence in the banking system of India. The following table gives an idea of the progress made by all the three Presidency Banks from 1895 to 1920.

(Figures in lakhs of rupees.)

Year.	Capital	Reserve	Govt. Deposits	Other Deposits	Cash	Investment	Dividend per cent
<i>Bank of Bengal</i>							
1895	200	68	184	677	422	132	10
1913	200	191	301	1824	840	319	14
1920	200	210	434	3398	1221	910	19½
<i>Bank of Bombay</i>							
1895	100	51	76	358	228	105	11
1913	100	106	200	1015	477	232	14
1920	100	120	349	2748	876	298	22
<i>Bank of Madras</i>							
1895	50	16	45	278	144	45	10
1913	75	73	86	805	219	177	12
1920	75	45	118	1579	505	211	18

As the table shows, in point of financial strength, the Bank of Bengal stood first, the Bank of Bombay second, and the Bank of Madras last. In the case of all the Banks there was scarcely any increase in the capital since they were started, and consequently a growing disproportion between the amount of capital and the total business transacted. The table also shows a steady growth in the amount of private deposits, especially during the War period. The Banks exhibited a strong cash position keeping on an average cash reserves much over 30 per cent of their liabilities. The rapid development of the business of the Banks can also be clearly seen from the progressive increase in their investments and the high rates of dividend declared by them, more particularly during the War period.

§ 9. Exchange Banks :—The Presidency Banks, as mentioned above, were prohibited from dealing in foreign exchange and raising funds outside India. But both these matters assumed greater and greater importance with the expansion of the country's foreign trade and there was ample room for another class of banks dealing principally with foreign exchange.

The Indian Joint-Stock Banks rarely engaged in this business for lack of the necessary training and experience and the want of access to the London money market. In the Pre-War period the only important Indian joint-stock bank which had a branch in London, like the Exchange Banks, was the Indian Specie Bank, but its London branch was apparently opened in order to facilitate the bank's dealings abroad in silver and pearls. The Alliance Bank of Simla (liquidated in 1923) and the Tata Industrial Bank (amalgamated with the Central Bank of India in 1923) also did a certain amount of exchange business.

Owing to the predominance of England in the foreign trade of India and the fact that London was the financial centre of the world, the early exchange banks established in India were due to English enterprise and had their head offices in London. But later on as the country was opened to every nationality branches of the principal banks in some countries other than England were started. The disturbance in the course of Indian trade and the important position attained by some foreign countries, that had not counted for much before in the international trade of India, acted as a stimulus to foreign banks opening their branches here. So that although the exchange banks carrying on business in India are mostly branch agencies of banks having their head offices in London, the number of those with their head offices in the continental countries, in the Far East, and in the United States has increased. The Exchange Banks can be classified as (a) those doing considerable business in India and (b) those which are merely agencies of large banks doing business all over Asia. Illustrations of the former are the National Bank of India, the Peninsular and Oriental Banking Corporation, the Chartered Bank of India, and as

illustrations of the latter we may mention the International Banking Corporation, the Imperial Bank of Persia, the Bank of Taiwan, the Yokohama Specie Bank, and the Banco Nazionale Ultramarino.

§10. The business and present position of the Exchange Banks:—Originally the business of the Exchange Banks was confined almost exclusively to the financing of the external trade of India. But in recent years most of them have also taken a considerable part in financing the internal trade at the places where their branches are situated. For example, the piecegoods trade in Delhi and Amritsar, and the leather trade of Cawnpore are largely financed by them. We have already seen that they no longer depend entirely on funds borrowed outside India, as latterly they have succeeded in attracting considerable private deposits in India. They do a certain amount of business on the lines of any ordinary bank. But their main business is financing the foreign trade by the purchase and discount of foreign bills of exchange. The import bills are negotiated in England and other foreign centres and are payable in India. But by far the greatest proportion of the bills in which the Exchange Banks deal are export bills. These bills are either documents on acceptance (D. A.), or documents on payment (D. P.). The D. P. bills, are held by the London offices of the Exchange Banks until they are retired or paid on maturity. The D. A. bills are generally discounted or rediscounted immediately after acceptance. They are rediscounted in the United Kingdom by the English and Scotch joint-stock banks or by the Bank of England. Thus the export trade of India is largely financed with the funds of the British Banks. Reference has already been made to the fact that the recently instituted practice of Government purchase of sterling enables the Exchange Banks to dispense with the system of rediscounting their bills in London to some extent, but by no means completely. The facility of rediscounting bills in the London money market where the rate of discount is usually lower than in India is a great advantage, as the Exchange Banks buy far more export bills than they can possibly hold until maturity. The absence of this facility in the

case of the Indian joint-stock banks makes it extremely difficult for them to compete with the foreign exchange banks whose large profits are protected by established and not easily assailable advantages.*

The purchase of Indian export bills by the Exchange Banks means a transfer of their funds to London. For bringing their funds back to India, the Exchange Banks were in the habit of freely purchasing Council Bills and Telegraphic Transfers in London, so long as this system lasted. Now they effect this transfer by selling sterling bills to the Government of India. There are other methods also by means of which they increase their funds in India, e. g. by cashing the import bills when they mature, the sale of drafts and telegraphic transfers in India for Indian students and travellers abroad and other persons requiring money to be remitted from India, by buying Rupee Paper in London and selling it in India and so on. In the last resort, when there is a strong favourable balance of trade, they import bars of gold and silver bullion and sovereigns from London, Egypt and Australia. In like manner when the balance of payments is against India the Exchange Banks either send gold or silver out of India or buy Reverse Councils if Government make them available.

In the financing of the import trade of India the more active part is played by the branches of the Exchange Banks outside India. The share of the Indian branches in the business consists primarily in collecting the import bills at maturity and in furnishing their branches with information as to the means and standing of the drawees of the bills. The import bills, unlike the export bills, are as a rule not rediscounted in India and thus the import trade is financed to a much greater extent than the export trade with the funds of the Exchange Banks.

Keynes points out that there is *prima facie* some danger to the stability of the Indian financial system in the fact that its money market is largely financed by funds raised not permanently, but for short periods, in a far-distant foreign centre.† However the greater success of the Exchange Banks in recent

* See Thakur op. cit. p. 73.

† See *Indian Currency and Exchange* p. 212.

years in attracting an increasing volume of funds in India itself, clearly brought out in the following table, has so far diminished their dependence on the London money market.

(In lakhs of rupees)

Year	No. of Exchange Banks	Deposits	Year	No. of Exchange Banks	Deposits
1870	3	52	1920	15	74,80
1890	5	7,53	1921	17	75,19
1900	8	10,50	1923	18	68,44
1910	11	24,79	1924	18	70,63
1913	12	31,03	1925	18	70,54
1918	10	61,85	1926	18	71,54

Although the Banks have thus succeeded in a very striking manner in attracting deposits in India it is desirable in the interests of safety that the sums borrowed on relatively short notice either in England or in India should not exceed the assets located there.* An adequate cash reserve to meet their deposit liabilities is also necessary. An important event in recent banking history in India is the entry into India of one of the English 'Big Five' which has been brought about by the acquisition of the business of Cox and Co. by Lloyd's Bank.

The following table gives a general view of the position of the Exchange Banks as it stood not long ago (on 31st December, 1926).

No. of Banks	Paid-up capital	Reserve and Rest	Deposits		Cash balances	
			Out of India	In India	Out of India	In India
	£. (1000)	£. (1000)	£. (1000)	Rs. (1000)	£. (1000)	Rs. (1000)
A† 5	9,644	10,471	73,533	51,07,24	14,234	7,32,99
B¶ 13	67,769	60,119	896,353	20,46,98	122,052	33,985

* Keynes: op. cit. p. 212-213.

† A=Banks doing a considerable portion of their business in India.

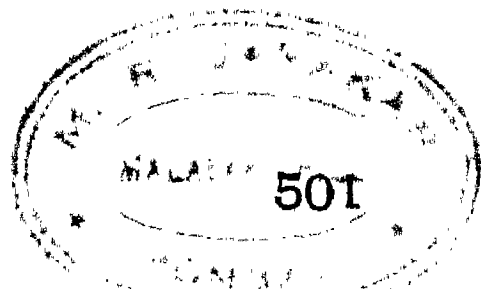
¶ B=Banks which are merely agencies of large banking corporations doing a major portion of their business abroad,

§ 11. History of Joint-Stock Banks:— The growing mass of internal commerce in India required organised banking of the modern type. Neither the Presidency Banks, which were semi-public institutions subject to various restrictions and which had branches only in a few large towns, nor the Exchange Banks which were mainly preoccupied with foreign trade finance, were able to supply the need of the country in this respect. The earliest bank of this description was the Bank of Upper India which was followed by the Allahabad Bank in 1865 and some more banks, one of which was the Alliance Bank of Simla (1874). In 1870, seven such banks were in existence. In 1894 the number rose to fourteen. Most of them were and continue to be under European management. The first bank for which Indians were responsible was the Oudh Commercial Bank started in 1881. In 1894 the Punjab National Bank was established mainly through the efforts of Lalla Harkishenlal who was also responsible for the establishment of the People's Bank in 1901. The People's Bank made great strides and at the time of its liquidation in 1913 it had nearly 100 branches and its deposits were over Rs. 1½ crores.* One of the results of the outbreak of Swadeshism in 1905 was a flood of new creations especially in Western India, U. P. and Punjab. It was to this epoch that the Bank of India the Bank of Burma, the Indian Specie Bank and the Bombay Banking Company owe their origin.

§ 12. Bank failures :— In the first few years great progress was made by most of these banks, but the business of many of them was of so unsafe and speculative a character and their cash reserves were so slender in proportion to their liabilities that it was easy for a trained and gifted observer like Mr. J. M. Keynes to predict speedy disaster, and Mr. Keynes had the melancholy satisfaction of very soon seeing his prophecy come true.† The failure of the

* See Thakur, op. cit. pp. 31-32.

† J. M. Keynes wrote in 1913 on the eve of the bank failures in India, "In the case of the smaller banks, dealing as they are with clients to whom banking is a new field and in a country where hoarding is still dominant, the cash balances seem, from available indications, to be hopelessly inadequate; and it is hard to doubt that in the next bad times they will go down like ninepins." *Indian Currency and Finance*, p. 225.



Peeples Bank on 20th September 1918 was followed by numerous other failure including that of the Specie Bank in November 1913. In the course of the year 1913-14 as many as 55 banks went into liquidation. The War and post-War boom gave another impetus to new flotations, and when the depression set in, a large number failures took place. Eleven banks failed in 1915, thirteen in 1916 and sixteen in 1918. The total number of failures from 1913 to 1919 was 89. Of the post-War failures, the most important was that of the Alliance Bank of Simla in 1923 which had far-reaching disastrous consequences. These failures had naturally a very adverse effect on banking business and did great injury to the industrial and commercial development of the country. Owing to the failures of 1913-17 no less than 34 per cent of the total trade of capital of the Indian Joint-Stock Banks was lost. But even more serious than the direct loss sustained by the depositors, most of whom belonged to the middle classes, was the shock to public confidence and the set-back to habits of investment.

§ 13. Causes of the Bank Failures :—The causes of the failures, particularly of those which occurred in 1913-14, were (1) slender percentage of cash to deposit liabilities, the average being 10 to 11 per cent; (2) unbusiness-like rates of interest offered in order to attract deposits; (3) absence of able managers and directors with the required knowledge of banking business and practice;* (4) fraudulent dealings on the part of some of the directors and managers; (5) absence of a proper proportion between the authorised and the subscribed capital, and between the subscribed and paid-up capital. The aggregate subscribed and paid-up capitals were 40 per cent and 14 per cent respectively of the authorised capital; (6) the gullibility of the depositors who were easily misled by the window—dressing of balance sheets and the payment of high dividend even from capi-

* "It was a case of an army growing into battle without any trained officers and without any orders from the General Staff." Findlay Shirras : *Indian Finance and Banking*, p. 336.

tal; (7) lack of palliative remedial action such as Government itself or quasi-Government agencies might have supplied.*

Some critics foolishly hinted that the bank failures demonstrated the incapacity of Indians to conduct organised banking of the modern type. But it must not be forgotten that such failures were a common feature of the early history of Joint Stock Banking even in England and the United States which are at the present time in the forefront in banking matters. Again as Mr. Doraswami remarks, "the path of Indian bank failures is strewn with the wreckage of European-manned institutions,"* and instances the failure of the first Bank of Bombay (1868) and the Arbuthnot Bank, to which we may add the recent big failure of the Alliance Bank of Simla.† Although fraudulent manipulation was proved in some cases, the principal cause of the failures was lack of experience and knowledge. The failures enforced the lesson that banking is no more "fool-proof" and "knave-proof" than certain currency systems and that it was necessary to minimize the risks of crises by improving the banking machinery.

The bank failures had at least one good effect, viz., that they removed the weak spots in the Indian Banking, although it must be noted that some deserving banks also failed along with many undeserving ones. They further demonstrated the necessity of a Central Bank like the Bank of England to guide the general banking policy in a time of crisis and to see to it that in normal times banking is conducted on sane and sound lines, e.g., by withholding accommodation or assistance in the case of ill-conducted banks. As Prof. Findlay Shirras points out, sound banking in India (as elsewhere) depends not merely on good laws but also on good bankers. The failures showed how necessary it was to make

* There was no tradition of co-operation between the banks themselves and it was suspected that the European banks did not show any great anxiety to come to the rescue of the Indian Joint-Stock Banks. For example, the Bank of Bengal refused to accommodate the People's Bank of India even on the security of Government Paper. There was also a want of co-operation and coordination between Indian Banks themselves.

† See S. V. Doraswami, *Indian Finance, Currency and Banking*, p. iii.

suitable provision for thorough instruction in the theory and practice of banking. Equally important with good banking laws and well-trained bankers is wide publicity which would enable the public to make a shrewd guess as to the position of a bank's affairs at any given time. It is true that very few of the shareholders or depositors will be able to probe the mysteries of a balance-sheet however much it may be simplified in order to make it intelligible to them. But every opportunity must be given to those who wish to look closely into the affairs of the bank and it is much to be desired that the number of wide-awake, intelligent and critical people willing and able to exercise a close supervision on the management of the bank should come to be far greater than it is. It is also essential that the banks themselves should develop high and honourable traditions and a sense of responsibility to the public.

§ 14. Importance of adequate cash reserves.—The maintenance of sufficient cash reserves is the very A B C of sound banking. But it is the experience of most countries that banks learn this salutary lesson only after a reckless disregard of it has actually caused a series of disasters. Indian joint-stock banking has already paid very heavy school-fees in the shape of bank failures, but seems to have at last learnt the lesson thoroughly, and the laudable desire to maintain strong reserves has been latterly more and more in evidence. The table on the next page shows the manner in which the three main types of banks in India have interpreted their responsibilities in this connection.

The percentage for the Exchange Banks have been calculated on their deposits and cash balances in India only.

The table shows that, while the cash position was deteriorating universally in the pre-War period, it was on the whole more satisfactory in the case of the Presidency Banks, less so in the case of the Exchange Banks and least satisfactory in the case of the Indian Joint-Stock Banks.

A comparative statement exhibiting the percentage of cash to liabilities on deposit of the several classes of Banks on 31st December of each year :—

	1904	1908	1910	1913	1917	1920	1923	1925	1926
1. Presidency Banks (since 1921 The Imperial Bank)	40	33	31	36	45	30	18	21	26
2. Exchange Banks doing a considera- ble portion of their business in India	29	17	16	19	40	30	19	13	14
3. Exchange Banks which are agencies of large Banks do- ing business all over Asia.	34	27	21	17	35	58	27	15	17
4. (A) Joint-Stock Banks (having ca- pital and reserve 5 lakhs and above)	12	15	11	18	25	23	17	19	15
4. (B) Joint-Stock Banks (having ca- pital and reserve between 5 lakhs and 1 lakh )	...	...	...	16	21	18	19	20	24

The lessons of the Bank failures of 1913-14 seem to have been taken to heart by all classes of the Banks especially by the Indian Joint-Stock Banks as shown by their improved cash position, though this was partly due to the panicky conditions created by the war which required stronger cash reserves than normally. Naturally since the end of the war the cash position has been somewhat less strong than in the war-period (except in the case of Exchange Banks doing only a small portion of their business in India which do not count so much for our present purpose).

The further decrease in 1923 seems to have been at least partially due to conditions of monetary stringency.

§ 15. Growth of Joint-Stock Banking:—The following statistics* give a general idea of the progress of Joint-Stock Banking in India during the last sixty years or so :—

Capital Reserve, Deposits and Cash Balances of the Principal Indian Joint Stock Banks on 31st December each year.

Class A:—Banks with Capital and Reserve of Rs. 5 lakhs and over. (in Lakhs of Rupees).

Year	No. of Reporting Banks.	Paid-up capital	Reserve and Rest	Deposits	Cash Balances.
1870	2	9.8	1.8	13	5
1880	3	18	3	63	16
1890	5	33	17	2,70	55
1900	9	82	45	8,07	1,19
1910	16	2,75	1,00	25,65	2,80
1913	18	2,31	1,32	22,59	4,00
1914	17	2,51	1,41	17,10	3,53
1915	20	2,81	1,56	17,87	3,99
1918	19	4,36	1,65	40,59	9,48
1920	25	8,37	2,55	71,14	16,30
1921	27	9,38	3,00	76,89	15,65
1922	27	8,02	2,61	61,63	12,03
1923	26	6,89	2,84	44,52	7,37
1924	29	6,90	3,80	52,50	11,29
1925	28	6,73	3,86	54,49	10,09
1926	27	6,61	4,08	59,61	9,11

Class B:—Banks with Capital and Reserve between Re. 1 lakh and less than Rs. 5 lakhs,

1913	23	39	11	1,51	24
1914	25	42	13	1,26	27
1915	25	45	9	91	20
1918	28	48	14	1,55	36
1920	33	61	19	2,33	41
1921	38	77	23	3,26	43
1922	41	83	27	3,37	56
1923	43	81	30	3,26	61
1924	40	72	34	2,66	34
1925	46	80	37	3,41	67
1926	46	83	39	3,45	82

* Statistical Tables relating to Banks in India (1928) Table No. 3,
I. E....64

ensure that proper practices were being observed and particularly to detect at an early stage transactions detrimental to the interest of depositors and shareholders and by fear of detection to prevent them. Dr. Slater and Sir P. C. Mitter gave evidence in a similar strain. The Committee did not make any definite recommendations on the matter but noted the argument against such Government control that, the sense of responsibility of banks and bank directors would be lessened and would lead to loss of efficiency, and that the best basis for sound and permanent advance lay in competition, publicity and the encouragement of private enterprise. Another argument against Government control of banks is that, while relaxing the sense of responsibility of the banks themselves, it would throw the odium of failure or mismanagement on the Government.

The subject of banking legislation came recently before the Council of State when Sir Ebrahim H. Jaffer moved a resolution on the 10th of March 1926 asking for an enquiry into the question. In the correspondence that has recently passed between the Government of India and the Provincial Governments on the suggestions made by the External Capital Committee, the subject of banking legislation was raised by the Bombay Government. And it also came up in the Central Legislature, when an amendment was added to Mr. Haji's resolution in 1927, asking for an enquiry into Indian banking. The Committee of enquiry has, however, not yet been appointed.* In view of the special conditions in India and the great importance to the country of banking development on sound and progressive lines it is clear that legislation on the general lines proposed above is essential. Far from hampering the growth of legitimate banking wise legislation ought to promote it.

* Banking legislation is apparently necessary not only for protecting the depositors and shareholders from unscrupulous banking management, but also for securing the protection of the banks themselves from irresponsible criticism. The venomous attacks to which the Central Bank of India has been subjected in certain quarters has brought this aspect into prominence, and it is suggested that some steps are necessary for the defence of banks against persons spreading false rumours to its detriment.

§ 17. The business of Indian Joint-Stock Banks:—The business of the Joint-Stock Banks in India is the usual one of receiving deposits, advancing loans, negotiating and collecting bills, etc. The rates of interest charged vary according to circumstances. The advances are made in the form of discounting local and inland bills, opening cash credit accounts etc. In the bigger towns, where stock-exchange securities are available, a large portion of the advances is made against them. In the interior, however, where such securities cannot be had, advances are made on the hypothecation of agricultural products, such as grain, cotton etc. Piecegoods and other commodities are also accepted sometimes as collateral. Short-term or periodical credit is supplied to mills and factories, generally against the security of stock-in-trade or some other suitable security. Sometimes, though rarely, mortgages of properties are also accepted as security. The Indian Banks do not generally rediscount their bills nor do they do the business of bank acceptances. These functions are left to the foreign banks. They do agency and safe custody work and transfer funds from one place to another on behalf of their clients. They buy and sell shares and other stock exchange securities for the public and thus help in the development of the investment habit, though this kind of work is not quite so well organised nor conducted on such a large scale as is usual with European Banks.*

The Indian Joint-Stock Banks have not made much progress in pushing their business in the mofussil areas. Their activities are concentrated in the Presidency towns, the large sea-ports and the more important commercial centres up-country, which offer opportunities for profitable investment of banking funds. Whenever they have branches these act merely as feeders of the head offices, situated in the chief commercial cities. The funds which they collect cannot be employed in local investments because the requirements as regards security cannot be easily satisfied in the mofussil. The result of this is that the rates on deposits at branches are governed more by the demand for investment in the bigger towns than in the locality itself; and

* Thakur : op. cit. pp. 66-67.

the work of supplying local banking needs is thus left to private bankers. This explains the slow development of branch banking in India and the disparity of rates of interest in the bigger towns and the mofussil.*

§ 18. Clearing Houses.—The system of 'clearing houses' was introduced in England towards the last quarter of the 18th century. It made possible the easy adjustment of countless cross claims without actual use of cash or money. The existence of this system explains to a large extent the phenomenal development of the cheque system in England and other countries. For the greater success of this system, it is necessary that one of the member-banks of the clearing house should act as the settling bank or the 'banker's bank' the other banks keeping a balance with it so that the settlement of cross claims is rendered more easy and complete.

The principal clearing houses in India are those of Calcutta, Bombay, Madras, Karachi and Rangoon. Clearing houses have also been established in Delhi, Simla, Ahmedabad and Colombo. The Imperial Bank of India has in view the establishment of more clearing houses at Amritsar, Rawalpindi and Peshawar. At many places where there is no clearing house, a system is in vogue of clearing accounts by giving cheques on the Imperial Bank in payment of balances due between the banks in the place. The Imperial Bank, the Exchange Banks, the English banking and agency firms and the leading Indian joint-stock banks are most of them members of clearing houses, and at each centre the Imperial Bank acts as the settling or banker's bank. A representative of each member-bank attends the meeting of the clearing house on each business day at a certain time. Since all the members have an account with the Imperial Bank the final balance left over after the cancellation of cross claims is usually settled by cheques and book entries, thus dispensing with cash in any form. The clearing house returns given below may be taken as some indication of the steady growth in the business of banking and the expansion of trade. The use of the cheque system, however, is

* See Gubbay : op. cit. pp. 5-9.

still in its infancy, being practically confined to the commercial towns. Nevertheless, the cheque is gradually finding its way even in the mofussil areas and the tendency has been especially marked since the establishment of a number of branches by the Imperial Bank. The cheques issued by the Co-operative Banks are also familiarising the public in the up-country districts with the new system.

The following figures* show the steady growth in the cheque system.

Clearing House Returns.

(Total amount of cheques cleared in crores of rupees)

Year	Amount	Year	Amount
1900	2,12	1921	20,21
1905	3,03	1922	20,22
1910	4,65	1923	18,76
1913	6,50	1924	17,77
1918	13,95	1925	17,69
1920	31,49	1926	15,91

To popularise and extend the clearing house system, more facilities must be given for the clearing of cheques of private firms up-country and the privileges of the clearing house extended to registered private banks of suitable status. The use of cheques, although it is growing, is far from being commensurate with the vast size of the country and its population. One of the hindrances to the growth of the system is wide-spread illiteracy. Besides, in order to write a cheque a person must not only be literate but must also know English. This is capable of being remedied if the joint-stock banks modify some of their methods and make use of the vernaculars in their transactions, particularly in respect of cheques, pass-books and deposit receipts.† But the greatest hindrance is the deficiency of banking facilities.

* Tables relating to Banks in India (1927)

† The recent abolition of the stamp duty on cheques is a measure intended to encourage the use of cheques.

§ 19. Postal Savings Banks etc:—Government Savings Banks were established in the Presidency towns between 1833 and 1835. In 1847 District Savings Banks were instituted in connection with certain select district treasuries. The Post Office Savings Banks were opened in all parts of India in 1882 and 1883 and absorbed the District Savings Banks' business in 1886 and that of the Presidency Savings Banks in 1896. The Government Savings Banks are, therefore, at present a department of the Postal administration. Government do not maintain any specific cash reserve for meeting their deposit liabilities, which constitute therefore an unfunded debt used for capital expenditure. The Postal Savings Banks provide the people of the middle and lower middle classes with a secure means of depositing their small savings, for which the general balances of the Government constitute a sufficient security. In 1914 Government offered increased facilities to depositors by raising the limit of the amount of the annual and total deposits permissible to an individual depositor as well as by helping the depositors in their investments in Government securities. This resulted in attracting large deposits, especially because public confidence in private banks had been badly shaken on account of the bank failures in 1913-14. The War, however, gave a temporary set-back to Savings Banks deposits, although there has been an improvement in the position recently, as seen from the following table:—

The growth of the Post Office Savings Bank Deposits.

Year	No. of Banks at the end of the year	No. of Depositors	Total deposit balances with the Govt. (in crores of rupees).
1913-14	9,824	1,639,000	23.16
1914-15	10,161	1,644,074	14.89
1918-19	10,587	1,677,407	18.22
1922-23	10,730	2,043,502	23.19
1923-24	10,535	2,039,314	24.78
1924-25	10,727	2,164,473	25.63
1925-26	11,162	2,317,390	27.23
	...	.....	29.83

These figures show that the pre-War amount of savings left by the public with the Post Office has been exceeded since 1922-23, though the position is less satisfactory than it looks if we consider the fall in the purchasing power of the rupee. There is a considerable scope for the expansion of Post Office Savings Banks, seeing that there were only 11,160 Savings Banks, for nearly five lakhs of villages in British India, so that in the case of a vast number of villages the nearest Savings Bank is several miles away, making it highly inconvenient for the village folk to deposit their savings in it.

In recent years there have been several forms of investment open to the public which have come into competition with the Post Office Savings Banks. For example, the War loans attracted many people who would otherwise have deposited their money with the Post Office Savings Banks. Other competitors are the Co-operative Credit Societies, the Imperial Bank and the Exchange and Joint-Stock Banks.

In spite of the emergence of all these rivals the Post Office Savings Banks will still succeed in tapping the savings of the people in a considerable measure, especially if further steps are taken to attract deposits. Among the suggestions made in this behalf are (1) a higher rate of interest on deposits more in correspondence with rates obtainable elsewhere; (2) a further relaxation of the restriction on the amount deposited annually and the limit on balances, subject to suitable precautions regarding sudden withdrawals; (3) the acceptance of deposits in the form of cheques (withdrawals not being allowed for a certain interval sufficient for encashment.)

The Post Office comes into contact with the savings of the people in another way, viz., through the Cash Certificates. Since the time of the War a Government Loan branch has also been usually tacked on to the Post Office. As regards the Post Office Cash Certificates the system is capable of being extended and further popularised so as to be able to finance a considerable portion of the Provincial capital expenditure. In 1927-28 the amount of the Postal Cash Certificates outstanding was Rs.

30.71 crores, whereas it was only 13.12 crores in 1924-25 and 8.88 crores in 1917-18, when the system was first introduced. In order further to popularise the Cash Certificates, Profs. Wadia and Joshi suggest that, as it is not possible to open a Post Office in every village, the village patel and the accountant who collect the land revenue could conveniently undertake the business in connection with the Cash Certificates, which may also be accepted at their realisable value in payment of land revenue. This will encourage thrift and habits of investment and avoid the large amounts paid annually as land revenue lying idle with the cultivator.*

§ 20. Effects of War on Indian Banking :—One of the effects of the War on Indian Banking was a remarkable increase in bank deposits. The total bank deposits of all the banks (the Presidency Banks, Joint-Stock Banks and the Exchange Banks)† amounted to 97.51 crores in 1913, 160.96 crores in 1917 and 224.97 crores in 1926. The respective shares in the total deposits in 1926 were as follows. (1) Imperial Bank of India, 37 per cent, (2) Exchange Banks, 33 per cent, and (3) the Indian Joint-Stock Banks, 30 per cent.

The large War profits made by some of the industries, like the cotton-mill and jute-mill industry, naturally increased the cash deposited with the banks. In addition to this the banks gave credit both to Government and private individuals and bodies in connection with the issue of and investment in War Loans and Treasury Bills. The banks gave credit to Government by themselves subscribing to the War Loans and the Treasury Bills; and Government drew upon this credit by issuing cheques on the banks to its creditors from whom heavy purchases of war materials etc. had been made. These cheques were in their turn carried to their accounts at the banks by the Government's creditors. The banks thus found that their deposits increased by the amount of their subscription to the Government Loans. The banks helped private persons and

* See Wadia and Joshi, *op. cit.* p. 359.

† In the case of the Exchange Banks only the deposits in India are taken into account.

bodies to invest in War Loans and Treasury Bills by opening deposit accounts with them. Thus both these sets of causes served to increase enormously the total amount of the deposits.

Another effect of the War was the worsening of the pre-War situation as regards the smallness of the capital of the banks in relation to the business transacted. This was due to the excessive anxiety of the banks to make larger and ever larger net profits by as rapid a turnover of their capital as possible.

Further, the War witnessed a very considerable growth in the cash reserves of the banks, partly owing to the increase in the deposits and partly to the necessity felt by the banks of maintaining stronger reserves as a safety measure under the abnormal War conditions and as a result of the banking crisis of 1913-14, the memory of which was still fresh and vivid. There was also a considerable increase in the investments of the banks, partly due to the great activity of the export trade, but primarily as a result of the banks' investments in War Loans and Treasury Bills. The War brought higher dividends, tighter money and high bank rates, and a great increase in the amounts of cheques cleared. Lastly, the experiences of the War imparted a greater urgency than ever to the question of a Central Bank, whose necessity had already been clearly indicated by the crisis of 1913-14.

§ 21. Case for Central Banks:—The International Financial Conference which met at Brussels in 1920 passed a resolution that "In countries where there is no Central Bank of Issue one should be established." Underlying this resolution is the idea that there is a close connection between the maintenance of financial stability and a central banking organisation. The advice embodied in this resolution has in the last few years been widely followed in the European countries, and the United States, till lately the home of decentralised banking.* In India the opinion had been gaining ground for a long time that a Central Bank was essential in the country for various reasons. By the force of circumstances Government had come to take upon themselves important functions such as note issue, management of cash balances, the regulation of foreign exchanges etc. and it was

* See Kisch and Elkin : *Central Banks*, p. 2.

felt that these functions are best performed by a Central Bank. Again, it was a great source of weakness that these functions should be divorced from banking proper. This divorce led to the keeping of two distinct reserves, viz., Government's reserves and Bankers' reserves, with ill-defined relations between the two, and it made the monetary system highly inelastic. The absence of a Central Banking authority further led to a general lack of direction in the banking policy of the country. Though there was the "multiple reserve" system in theory, that is to say, the various banks kept their own reserves, in practice these reserves were hardly adequate, and the danger was that in a crisis everyone would count upon every one else. The bank failures of 1913-14 added to the strength of this argument. Other advantages from a Central Bank would be a moderation of the wide fluctuations of the bank rate and a mitigation of its normal high level through an enlargement and co-ordination of the banking resources of the country. The Central Bank would also provide adequate rediscount facilities, so that, the other banks would be in a position easily to liquefy their assets—a facility which would increase their credit. A Central Bank would further take over from Government officials the responsibility for a variety of financial and semi-financial duties for the discharge of which they were ill equipped. The absence of expert advice and experience in India had resulted in the centre of power in financial matters being shifted to the India Office and the India Council, which, however, were not adequately in touch with conditions in India. The Central Bank would get over this difficulty by providing trained experience and advice on the spot and it would also be useful as a buffer between the Secretary of State and public criticism. To these arguments may be added another one which has come to the fore of late. The introduction of a gold bullion standard in India has imposed or is going to impose on the currency authority, the obligation to buy and sell gold at a fixed parity on demand and to allow the free inflow and outflow of gold. The unlimited obligation to provide gold (or gold exchange) at a fixed price requires that the currency authority should be in a position to check a drain on its gold reserves by raising its rate of discount. On the other hand,

if gold is being imported, the currency authority will lower its discount rate. The manipulation of the discount rate so as to maintain currency stability is a function which falls peculiarly within the sphere of a Central Bank. A central Banking organisation is further calculated to help a fuller, wider and more effective use of the Government balances for commercial and industrial purposes. A Central Bank would also extend banking facilities by opening numerous branches (see, however, §39 below) and arranging for a continuous reduction of remittance charges from one part of the country to another, to the great benefit of the commercial community. Another advantage to be expected from a Central Bank would be a wider diffusion of sound and reliable banking practice. Lastly, the maintenance of the stability of the purchasing power of money is being increasingly recognised to be a world problem requiring the co-operation of the principal countries of the world. This co-operation would be best attained, if each country equipped itself with an efficient Central Bank.¶

§ 22. History of the Proposal:—The idea of a Central Bank for India is almost a century old. As early as 1836, a large body of merchants interested in the East Indies submitted to the Court of Directors a project for a great banking establishment for British India and claimed the following advantages for the scheme. (1) That it would facilitate the use of English capital for financing English commerce; (2) give stability to the monetary system of India; (3) and would be convenient to the East India Company in connection with its financial arrangements, especially the management of revenue receipts in India and the remittance of Home Charges. The basis of the Bank of Bengal, it was urged, was too narrow for such a customer as Government. The definite establishment of the three Presidency Banks put an end to the idea that had been in the air for some years of turning the Bank of Bengal into a Bank of India. The scheme of constituting an all-India Bank by the amalgamation of the Presidency Banks came to the front for the first time in 1867, when it was proposed by Mr. Dickson,

¶ See Kisch and Elkin: *Central Banks*, pp. 3-5.

Presidents and the Secretaries of Local Boards as representatives of the shareholders; (3) The Controller of Currency or some other officer nominated by the Governor-General; (4) and lastly, not more than 4 non-officials nominated by the Governor-General-in-Council to represent the interests of the general tax-payer and the public. Representatives of any new Local Board that may be constituted may be added at the discretion of the Central Board. The Controller of Currency and the Secretaries of the Local Boards are not entitled to vote. They are only sitting members. The Controller of Currency is the representative of the Government and acts as the guardian of its interests. The Governor-General-in-Council is entitled to issue instructions to the Bank in respect of any matter, which in his opinion vitally affects financial policy or the safety of the Government balances. If the Controller of currency or any other nominated officer gives notice in writing to the Managing Governors that the Governor-General-in-Council considers any action proposed to be taken by them to be detrimental to the Government, such action cannot be taken without the written permission of the Governor-General.

The duties of the Central Board are to deal with matters of general policy, to exercise general powers of control over the Local Boards, to determine the distribution of funds and the fixation of the Bank Rate and to be responsible for the weekly publication of the Bank's accounts.

The Local Boards on the other hand deal with the ordinary day-to-day business in their respective territories. For the current general (central) management there is a smaller working body consisting of three members of the Central Board, of whom one is the Controller of Currency.

A novel feature is that the Bank is allowed by the Act to establish a London Office. It is not however permitted to deal directly with the public in foreign exchange, though it may transact business in London on behalf of the Indian Government including the Secretary of State, public bodies, other banks and the old customers of the Presidency Bank.

§ 25. Functions of the Imperial Bank:—The Act follows the old Presidency Banks Act of 1876 in defining absolutely the class of business in which the Bank may engage, though the old restrictions are modified in some minor points, especially in regard to certain limited powers of access to the London Money Market and dealing in foreign exchange.

Functions allowed to the Bank: (1) Investments in certain specified securities of the Government of India, United Kingdom Port Trust Bonds, certain Municipal Corporation Bonds and those of State-aided Railways and of District Boards. (2) Advancing of money against any of the above securities. (3) Advancing of money against accepted bills of exchange and promissory notes, against goods or documents of title thereto deposited with or assigned to the Bank. (4) Drawing, accepting, discounting and selling bills of exchange and other negotiable securities payable in India or Ceylon; and, subject to the direction of the Governor-General-in-Council, the discounting, buying and selling of bills of exchange payable outside India for, from or to such Banks as may be approved. The Bank is allowed to draw bills of exchange and grant letters of credit for the use of parties whose estates are being administered by the Bank and also for private constituents or customers for bona-fide personal needs. (5) Borrowing funds in India and receiving deposits, receiving securities for safe custody and collecting interest thereupon, buying and selling gold and silver etc. (6) The London office is allowed to borrow money in England for the purpose of the Bank's business upon the security of assets of the Bank, but is not to open cash credits, keep cash accounts or receive deposits in London except from the former customers of the Presidency Banks. The Act provides for an agreement between the Bank and the Secretary of State for India to last for ten years being terminable thereafter after one year's notice.

§ 26. Functions as a public Institution—The functions of the Bank as a Government Bank are as follows:—

(1) To undertake all the general banking business of the Indian Government, and to accept payments and make disburse-

ments for Government. The Bank holds all the Treasury Balances at headquarters and at its branches. (This involved the abolition of the Reserve Treasury System.) (2) The Bank manages the public debt in return for a specified remuneration. (3) The Bank was required to undertake to open 100 new branches of which the Government of India might determine the location of one in four. Before January 1921 when the Imperial Bank Act came into force the Presidency Banks had between them 59 branches. To these 102 new branches were added by 31st March 1926, making a total 161 branches. Of the new branches 36 are in places where there was previously no other bank, while 61 of the remaining 66 were opened at places where there was a Government Treasury. In all, 89 of the new branches are at places where there is a Government Treasury.† (4) The Bank is expected to give the public every facility for the transfer of money between its branches at reasonable rates approved by the Controller of Currency. The maximum rate for the transfer of amounts of Rs. 10,000 and over was fixed at one anna per cent (instead of the usual four annas per cent), but recently in order to assist other banks and to encourage them to effect their transfers through the Imperial Bank the rate for banks has been reduced to half an anna per cent. Government was to cease remittance of funds for the public between any two places where the Imperial Bank carried on business. (6) The London Office of the Bank which was started in January 1921 has taken over a portion of the business of the Government of India which was previously in the hands of the Bank of England, e. g. the current account of the High Commissioner for India.

§ 27 Business prohibited to the Bank:-(1) The restrictions as to dealing in foreign exchange and raising funds in London in their relaxed and modified form have been already noted. (2) Loans or advances upon mortgage or otherwise, upon the primary security of immovable property, or the documents of title relating thereto, are expressly prohibited, but allowed against such a collateral (secondary) security if the main security is of the type noted already (see above). (3) The amount which may

† Report of the Controller of the Currency, 1925-26. pp. 20-21.

be advanced to any individual or partnership or firm by way of discount or on any personal security is limited under bye-laws sanctioned by the Government. (4) Loans or advances cannot be granted for a longer period than six months. (5) Discounts cannot be made or advances on personal security given unless such discounts or advances carry with them the several responsibilities of at least two persons or firms unconnected with each other in general partnership.

§ 28. Financial position of the Imperial Bank:—The following tables between them give an idea of the nature of the heritage into which the Imperial Bank has entered and afford a synoptic view of its resources and functions:—

*Capital Reserve, Deposits and cash balances of the Imperial Bank.**

(In lakhs of Rupees)

31st Dec. Year	Paid-up capital	Reserve & Rest	Public Deposits	Private Deposits	Cash balances
1870	3,36	25	5,43	6,39	9,96
1890	3,50	97	3,59	14,76	12,96
1910	3,60	3,31	4,23	32,34	11,35
1913	3,75	3,73	5,88	36,48	15,37
1918	3,75	3,44	8,64	50,97	17,07
1920	3,75	3,77	9,02	78,01	26,03
1921	5,62	4,14	6,80	65,77	13,60
1922	5,62	4,33	14,15	57,00	15,07
1923	5,62	4,55	8,56	74,19	15,01
1924	5,62	4,80	7,50	76,71	15,60
1925	5,62	4,92	5,46	77,83	17,46
1926	5,62	5,09	6,45	73,89	20,90
1927 (30th June)	5,62	5,07	10,04	73,17	22,83

* Figures prior to 1921 represent the totals of the three Presidency Banks.

Statement of the position of the Imperial Bank of India for the week ending 28th December 1928.

In lakhs of rupees and decimals.

Liabilities		Assets	
Subscribed capital	1,125.00	Government securities	1,906.56
Capital paid up	562.50	Other authorised securities under the Act.	272.33
Reserve	517.50	Loans	2,138.00
Public deposits	879.84	Cash Credits	2,667.10
Other deposits	6,957.65	Inland Bills discounted and purchased	1,237.21
Loans against securities per contra		Foreign Bills discounted and purchased	39.93
Loans from the Govt. of India under section 20 of the Paper Currency Act against inland bills discounted and purchased per contra	700.00	Bullion	.....
Contingent liabilities	160.56	Dead Stock	284.04
Sundries	.....	Liability of constituents for contingent liabilities per contra	99.58
The above balance sheet includes:—		Sundries	
Deposits in London	£932,200	Balances with other Banks	11.66
Advances in London	£908,700	Cash	1,121.64
Cash and Balances at other Banks in London	£89,800		

Percentage of Cash to liabilities 12.89.

Bank Rate 7 per cent.

Some of the items in the above statement may be further explained.

(1) Liabilities:—The "Public Deposits" stand for Government Cash Balances left with the Bank free of interest. "Other Deposits" are private deposits and include the deposits of the Exchange Banks, Indian Joint-Stock Banks and semi-public corporations and those of traders and private people. "Loans against securit-

ies per contra " represent the borrowing of the Bank against some of its authorised securities included on the assets side. "Loans from the Government of India under Section 20 of the Paper Currency Act" are in connection with the issue of seasonal (paper) currency against inland bills of exchange during the busy season. *

(2) Assets:—" Government securities " represent the investments of the Imperial Bank in Government Loans, while " other authorised securities " represent the holdings allowed by the Act. Then follow " Loans " " Cash Credits " and " Inland Bills " which represent the commercial investments of the Bank or accommodation granted to business men for short period not exceeding six months. § " Inland bills discounted and purchased " represent the discounting of *Hundis* and internal trade bills and arise in connection with the discounting or rediscounting of their *Hundis* by the shroffs at the Imperial Bank. The purchase and discount of " Foreign Bills " is undertaken by the Bank for its customers only, as already explained. Otherwise the Imperial Bank is not allowed to deal in foreign exchange. " Balances with other Banks " refer to accounts opened with other banks by the Imperial Bank in order to facilitate the collection and payment of the cheques. The last item " Cash " is very important and refers to the cash in hand or cash that is available for meeting the liabilities of the Bank such as deposits, loans etc. The percentage of cash to liabilities indicates the strength of the Bank to meet its liabilities. †

* See pp 395-96 above.

§ The difference between loans and cash credits is that while the loan is a fixed amount for the period for which the advance is made, the cash credit is usually granted upto a stated maximum beyond which the borrower cannot ask for money, but within which he can pay up or withdraw as often as he likes during the currency of the arrangement. Though the yield from cash credits may be less than from an equal amount given as a loan the former is more convenient to borrowers. See K. T. Shah : *Indian Currency, Exchange and Banking*, p. 329.

† For a fuller explanation of all the items see B. R. Rau, *Present-Day Banking in India*, pp. 23-24.

§ 29. Points of criticism against the Imperial Bank :—The Imperial Bank has been made the target of much adverse criticism. We shall here mention some of these points of criticism. First of all it is objected that the Imperial Bank is not a genuine public corporation or a State Bank. It is a private concern and especially open to suspicion on account of the strong representation of European interests on it which limits the utility of the Bank to the Indian commercial and industrial interests. The Imperial Bank has merely perpetuated the old management, the old politics and the old traditions of the Presidency Banks. The English management is unsympathetic and is also unable to understand the needs of the Indian merchants and industrialists.* The Imperial Bank is further subjected to the criticism which has been raised against European managed concerns in general, viz., that they do not care to provide for the training of Indians.† The scheme of Indian apprentices has not been worked so as to give full satisfaction. The Bank has indeed just made a beginning in filling responsible posts by Indians but it has not gone nearly as far as it might in this direction. The Imperial Bank has also been freely charged with discriminating against Indian firms and Indian institutions and showing undue partiality to European firms and European institutions.

The representation of Indian interests by the nomination on the Central Board of four non-official Indians is not considered sufficient and the public demand is that they should be elected by the Assembly.

The Imperial Bank being a private concern, the State is deprived of the profits which it would have derived if it had been a State Bank. Nor is there any arrangement for a division of profits between the Bank and the State. The prestige and the material assets of the Bank, it is argued, depend to a large extent on its connection with the State, which is therefore entitled to a portion of the profits. The State's claim to a share in the profits is, however, not merely a matter of *quid pro quo*. Its more important justification is that it prevents the Bank from be-

* Thakur : op. cit. pp. 56-60.

† See Vol. I, pp. 490-91.

ing lured into unsound methods of business.* The Bank has been recently declaring very high dividends (as much as 16 per cent) and this ill squares with the primary object for which the Bank exists, viz., the promotion of national welfare. The Central Board has been found by experience to be too inactive and wanting in initiative. At best moreover it can merely lay down a policy but cannot see it carried out. It has degenerated into a mere board of trustees, each member of which is concerned with watching the interest of his own ward or sphere. There is no action by united impulse for furthering general welfare on the part of the Board as a whole. The powers of the Board are negative in character and not sufficient for evolving a continuous and constructive programme of banking development. §

The control of the State over the Bank is not as effective as it ought to be, as the Controller of Currency is expected to interfere only when Government interests are at stake. The branch banking policy of the Bank has not been very successful. Branches have sometimes been established at places where there were already sufficient banking facilities and this has exposed existing banks to unfair competition at the hands of the Imperial Bank with its special privileges and its large command of Government funds.

Another group of criticisms is on the score of the limited functions assigned to the Bank and the consequent impairment of its utility. The Imperial Bank has little real resemblance with the Banks of Europe in relation to the banking and currency functions it performs for Government. In the case of the other Banks, with the exception of the management of the State Mint, everything else e. g. the management of the reserves, Government balances and note-issue etc., is left to the Central Banks. But in the case of the Imperial Bank, only the cash balances and the duties of a general banking nature have been handed over to it. The Paper Currency, the Gold Standard Reserve and the remittances to England for meeting the Home Charges are still managed by Government. Not having the power of note issue, the Im-

* Kisch and Elkin : op cit. p. 39.

§ Cf. K. C. Mahindra : *Indian Currency, and Exchange*, pp. 193-195.

perial Bank cannot effectively control the money market through its rate of discount as do the great Central Banks of Europe.

The monopoly of the Exchange Banks and the Government in the field of foreign exchange have been left practically intact. The fact that the Exchange Banks have prospered so well shows that the risky character of the business has been greatly exaggerated. Another restriction imposed on the Imperial Bank is that it cannot borrow without security or accept deposits outside India. This is no more than a concession to the jealousy of the Exchange Banks which also explains the exclusion of the Bank from foreign exchange business. Borrowing and receiving deposits abroad sometimes may be necessary for easing the situation in the Indian money market. Lastly, the Imperial Bank, though it is intended to be a co-ordinating agency, is still far from being a banker's bank in the strict sense of the term. The other banks do keep their reserves with it but only to a very limited extent. The result is that the Indian money market remains practically as inorganic as it was before the Imperial Bank was brought into existence.

§ 30. Bank Rate and monetary stringency :—"The Bank Rate is the rate at which the Imperial Bank will ordinarily advance money against Government security, while the Imperial Bank hundi rate is the rate at which the Imperial Bank will discount or rediscount first-class three months' bills. The Bazar Rates are those at which the bills of small traders are discounted by shroffs." The statistics on the next page have a bearing on various questions in connection with money-rates about to be discussed.

The close relation between the Bank Rate of the Imperial Bank, the Hundi Rate and the Cash Balances can be easily seen from the first of the tables below. The Bank Rate varies inversely with the Cash Balances. The balances get depleted during the busy season (November to June) when money is transferred upcountry to move the crops and they begin to swell during the slack season (July to October), when the money returns to the financial centres in payment for bullion or other commodities. Thus the Bank Rate varies with the intensity of the demand for money, which again depends upon the nature of the

TABLE I.

1st of	Cash Balances (in lakhs of rupees)	Bank Rate Per cent	Imperial Bank Hundi rate Per Cent	Bazar bill rate	
				Calcutta per cent	Bombay per cent
April 1927	15,31	7	7	10-12	10½
May „	14,94	7	7	10-11	10½
June „	18,95	7	7	10-11	10½
July „	32,36	5	5	9	7½
August „	32,22	4	4	9	6¾
Sept. „	30,37	4	4	9	6¾
Oct. „	28,09	5	5	9-10	7½
Nov. „	24,70	5	5	8- 9	7½
Dec. „	10,96	5	5	8- 9	8½
Jan. 1928	13,68	7	7	10-10½	9¾
Feb. „	14,08	7	7	10-11	10½
March „	11,67	7	7	10-11	9¾

TABLE II

The maximum, minimum and average bank rates of the Imperial Bank of India.

	1922-23	1923-24	1924-25
Maximum	8	9	9
Minimum	4	4	4
Average	5.91	6.11	6.24

harvest, the briskness of the demand for the great staples of agriculture (cotton, jute, wheat, rice, etc.) especially for export purposes, and the range of prices prevalent for them. We have already seen how the crops are financed in the earlier stages by the indigenous bankers and how a considerable volume

of business is thus brought by them to the Imperial and other banks who discount and rediscount the shroffs' Hundis. The demand for moving the crops occasions a seasonal stringency in the money market, which is also further emphasised by the great demand for currency which comes at the same time in connection with holidays, marriage ceremonies, etc. But apart from these causes accounting for seasonal stringency there are other factors responsible for the normal high money rate in India. We have already spoken about the part which the reserve treasuries played in causing monetary stringency. The transfer of large cash balances at the present time to the Imperial Bank has brought some relief to the money market. But the Government monopoly of note issue and its divorce from banking is responsible for a maladjustment between the supply of and demand for money. A certain element of elasticity has been imparted to the note issue by the provision for the seasonal issue of currency up to Rs.12 crores against inland bills of exchange, under the Paper Currency Act. But this amount has been fixed arbitrarily and its extension is widely desired by the commercial public. The monetary stringency has also been attributed to the heavy borrowings of Government in the money market since the War, which prevent the Imperial Bank from collecting sufficient surplus cash, and thus the money rates remain unduly high. The exchange policy of Government and the drastic deflation or refusal to allow the normal increase in currency has also added to the monetary stringency from time to time. But from the nature of the case this cause comes into operation only occasionally. On the other hand, the purchase of sterling in India and arrangements for cheap inland remittances and the starting of a fairly large number of branches by the Imperial and a few other banks have had the effect of lowering the pitch of money rates during the busy season to some extent. But the position cannot by any means be regarded as completely satisfactory. The normal rate for money is yet far too high and acts as a discouragement to business activity. A fundamental reason for the high rate is the scarcity of capital which is the direct result of the great poverty of the people. The income of the great majority of the people is so small that any saving is scarcely possible for

them. Another reason is that a considerable amount of potential capital takes the form of hoards which lie idle and sterile in the absence of adequate banking facilities to attract them into profitable investment. The question of hoarding is discussed in greater detail in a subsequent section below. Another characteristic of the money rate in India is the perceptible disparity in it at the three centres, Bombay, Calcutta and Madras leading to fluctuations in the prices of securities and reactions on trade movements. There are also wide fluctuations of the rate from one period to another during the year. Both these defects point to the need for a Central Banking Agency which would spread the available resources more evenly over the different parts of the country and the different seasons of the year.

§ 31. Relation between the Bank Rate and the Bazar Hundi Rate:—We have already remarked that the indigenous banker finances the movement of crops during the busy season largely from his own resources. He is, however, ultimately dependant upon the Imperial and the other Joint Stock Banks for additional funds he requires. Therefore in times of stringency the bazar rate for first class *hundis* follows the Imperial Bank Rate. As we have seen the Shroffs who do the Hundi discounting business, charge higher rates than the Bank Rate profiting by the difference between the two rates. Towards the beginning of the slack season the Bank Rate is generally higher than the Hundi Rate.* When money is easy the correspondence between the two rates is less close than when it is tight and the Shroffs may disregard the Bank rate and may underquote the Bank,† It should be noted in connection with the absence of the complete harmony between the two rates that the Shroffs rarely ever discount European paper and do not purchase foreign or sterling bills. "Neither do they

* "The hundi rate rises and falls with the bank rate proper though somewhat in advance of it and naturally so, for one is a discount rate and the other rate for day to day loans. Thus at the beginning of the busy season, the hundi rate would usually be higher than the bank rate; the reverse being the case when slack season is about to begin, so that the hundi rate may be said to be a sort of long distance single signal."

† See Shirras : *Indian Finance and Banking*, pp. 341-42.

lend money on Government paper or similar securities but confine their advances to the discount of hundis, to loans to cultivators and against gold or silver bullion." The Banks do not compete with the Shroffs for the purchase of traders' hundis and therefore there is often little apparent relation between the Shroff's Rate and the Bank Rate. The Shroff's reliance on Banking funds is not sufficiently continuous or sufficiently great for the two rates to be closely similar. The operations of the Shroffs still lie to a great extent outside the Banking system of the country and one of the problems of Indian Banking is how to rope in the indigenous banker in an all-pervading banking organization so as to ensure an effective control over credit and currency. We must however qualify the above statement by the remark that there is a growing tendency for a more intimate connection being established between the indigenous bankers and the Joint Stock Banking system. Although the difference of conditions and of securities subject to which business is transacted are responsible for a considerable disparity between the two rates, both the rates are governed by the same fundamental causes connected with the seasonal demand for currency.

§ 32. Methods of inland remittance:—In connection with the movement of crops during the busy season, the question arises as to how the large funds required at different times of the year in different parts of the country are provided for. Five main methods of inland remittance may be distinguished:—(1) Remittance by Hundis or cheques; (2) transfers through the Imperial Bank; (3) transfers through the Government Treasuries; (4) transfers of rupees by rail or road; (5) remittances through the Post Office.

(1) *Hundis or Cheques*:—We have already discussed the operations of the shroffs and their Hundi business. We have also spoken of the increasing use that is being made of the cheque and the part played by the machinery of Clearing Houses in facilitating payment by cheques.

(2) *Transfers through the Imperial Bank*:—The obligation of the Imperial Bank under its agreement with the Government

of India to give the public every facility for the transfer of money between its branches at reasonable rates is being increasingly utilised by the public. Most of the other Joint-stock Banks also issue banker's drafts on payment of a small commission.

(3) *Transfers through the Government Treasuries* :—Though Government Treasuries are primarily maintained for administrative purposes, they usually sell to the public " Supply Bills " drawn upon other treasuries, provided the latter have sufficient funds. If very large remittances are desired, " Currency Transfers " may be issued, which are payable out of the " Currency Chests " in which the Paper Currency Reserve is kept, while the " Supply Bill " is payable out of the ordinary Treasury Balances. If an amount is taken from a Currency Chest, an equivalent transfer from the Treasury Balances to the Currency Chest is made at some other Treasury.* A small commission is charged for these transfers. The banks and big merchants are taking increasing advantage of these facilities for cheap transport of funds. It has already been stated that Government have bound themselves not to issue currency transfers and supply bills to the public between any two places in which a Local Head Office or a branch of the Imperial Bank is situated. With the increase in the number of branches started by the Imperial Bank there will be a diminution of the amount of transfers through Government agency.

(4) *Transfers by rail or road* :—Though the actual transport of specie by rail or road is being gradually superseded by the methods described above, considerable amounts of rupees are

* Economy of metallic currency is promoted by the establishment of currency chests which contain a portion of the balance of the Paper Currency Reserve and are quite distinct from the treasury balances. They are required to be kept separately in separate chests, and their accounts are also outside the general treasury accounts. Into these currency chests are deposited the district surpluses when revenue is coming in and is in excess of the requirements of the district treasury in question. For all such deposits made by the district treasuries into its currency chest a corresponding transfer in the opposite direction is made at provincial headquarters from the currency balance held at the Currency Office to the treasury balance kept with the head office of the Imperial Bank of India. Wattal, op. cit. p. 220.

still sent by rail to cotton and jute areas for purchasing the crops from the cultivators and small merchants who insist on payment in silver coin. Even the 10-rupee note is of too high a denomination for ordinary petty purposes. As Stanley Jevons observes, "It is a feature of the present organisation of internal payments in India that actual silver coin is moved from place to place chiefly by railway to a far greater extent than in European countries. Coin very frequently has to be moved by Government and also by Banks. It so happens that the different harvests are ready to be moved at different times in different parts of India. The cotton crop is moved in December to April in Western and Northern India, the wheat crop in April, May and June in Northern India and the Burma rice crop in January to April, and the jute crop in August to December." Silver coin is thus moved many hundreds of miles backwards and forwards between different parts of India during the year. There is as yet no general tendency to replace coin by notes, and the cultivator still tends to keep his store of value in coin.

(5) *Postal remittances*:—Remittances by postal money orders serve a useful purpose so far as small sums are concerned. The Post Office has developed a system of setting payments in opposite directions against one another similar to that followed in the case of cheques. Remittance in notes through the Post Office early established its popularity and incidentally led to the adoption of the circle system for the regulation of Paper Currency.*

All these methods help in increasing the fluidity of money and prevent the rates for it at different places from being even more disparate than they actually are.

§ 33. *Industrial Banks*:—One of the great lacunae in the Indian industrial organisation is the absence of properly organised Industrial Banks. We have already shown how the various types of banking institutions existing in the country at the present time are unequal to the task of effectively financing industry and how special Industrial Banks are necessary for the

* See p. 389 above.

purpose.* The ordinary Joint-Stock Banks cannot combine very well the function of industrial, with commercial finance. At the same time, many of the new industries especially in up-country places, find it very difficult to get the requisite capital. The company promoter who has hitherto fulfilled the function of financing industry to some extent is looked upon with distrust by the investing public. The promoter does not carefully weigh the prospects of the proposed enterprise. He is concerned not so much with the success of the business as with the success of the issue in which he is interested. An Industrial Bank, on the other hand, would carefully investigate a proposition before consenting to finance it and will also be interested in seeing to it that the business is properly conducted.†

The first considerable attempt in Industrial banking was the establishment of the Tata Industrial Bank. It had raised high expectations and its failure occasioned much bitter disappointment. Its inability to 'make good' has been attributed to various causes, such as the following :—(1) It is said that it was over-staffed with an extravagant and inexperienced European agency.¶ (2) Again, it undertook foreign exchange business which was alien to its main function. (3) Its Directorate was too closely associated with the flotation of large enterprises during the boom period.§ (4) Lastly, it suffered from the lack of expert local advice in giving financial assistance to small concerns upcountry.

While the failure of the Tata Industrial Bank has discouraged the establishment of other banks, the need for Industrial Banks remains as urgent as ever. It seems, however, that at the present stage of India's development, it is necessary for the State vigorously to associate itself with industrial finance on some such lines as those adopted by Germany and Japan. The Industrial Commission note the following as the signal characteristics of the German Banks (Grossbanken) :—

* This section should be read together with pp. 482-84, Vol. I.

† See Thakur : op. cit. p. 315.

¶ See K. T. Shah : *Indian Currency, Exchange and Banking*, p. 367.

§ See Wadia and Joshi : op. cit. p. 390.

(1) High proportion of paid-up capital to total cash transactions so as to lessen the dependence of the Bank on outside deposits. (2) The readiness with which industrial and commercial business is financed and the active participation by the Banks in fresh industrial ventures by taking up or underwriting and eventually selling blocks of shares in these ventures. (3) The large measure of control exercised by the Banks over the businesses financed by them through their representatives and directors. (This has enabled the Banks to make these undertakings help themselves and one another, and to have at their disposal the wide range of technical knowledge and experience of the assisted businesses to aid them in deciding on the merits of further undertakings). (4) The Reichsbank or the Imperial Bank of Germany and the German Government make it their special business to extend such assistance as may be deemed necessary to the Industrial Banks.

With regard to Japan, the Industrial Commission point out that the speciality of Japanese banking consists in the close connection between the banks and the Japanese Government, which helps them directly and indirectly e. g. by extending guarantees of limited duration on the investments of the industrial bank* and in return exercise a certain measure of control by regulating their business, laying down conditions with regard to security accepted and the objects on which the loans are expended etc.

Industries in India would benefit materially by the introduction of a similar system of Industrial Banks. The Industrial Commission considered that the establishment of Industrial Banks was of sufficient national importance to justify Government assistance. Between the years 1918-1920 a number of Industrial Banks were started by private initiative, but what is wanted in India is not a series of scattered and unco-ordinated banks like these, but a Central Industrial Bank with a large number of branches. Instead of one giant Bank for the whole of India it would probably be desirable to establish one important industrial Bank in each of the major provinces. It would, however, be necessary to devise proper machinery for securing effective

* In the case of the Industrial Bank of Japan 5 per cent dividend for five years was guaranteed to the shareholders by the Japanese Government.

tive co-ordination between all the banks in a province by the institution of a Central Board "to strengthen, guide, and systematise their organisation. Expensive and expert staff may be engaged by such a Board."*

The Industrial Commission suggested that a properly constituted Industrial Bank in India would possess the following features :—(1) High paid-up share or debenture capital in proportion to the total business of the Bank. (2) Distribution of funds over a large number of interests instead of their concentration on a single interest or a group of financially interdependent interests. The main factor of safety in an Industrial Bank lies in the judicious limitation of each class of business to its proper proportions. (3) Careful scrutiny of loans on plant or machinery, buildings and land and the limitation of loans as far as possible to the provision of working capital. (4) Reluctance to provide initial capital at least during the earlier years of the Bank's career. (5) The Bank should not itself attempt to float companies though it may advise and assist in other ways persons who propose to do so.

§ 34. Financial Operations of an Industrial Bank :—The financial operations appropriate to an Industrial Bank may be outlined as follows :—(a) To receive deposits from the public for fixed terms, say, five years. (b) To advance long-term loans to customers on the security of their business or a mortgage of the company's assets.† (c) To receive loans e. g. from the Imperial Bank for fixed terms, to issue debentures or bonds from time to time. (d) Guarantee, accept or endorse the bonds or debentures of private firms or corporations carrying on industrial enterprises in which the bank is financially interested and on which it is represented. It is important that the bank should be adequately represented on the directorate of such concerns and should be

* Thakur, op. cit. p. 326.

† These operations are like those of land mortgage banks except that the Industrial Banks take part in the management of the actual business and grant loans for periods generally not exceeding twenty years, while the Land Mortgage Banks may grant loans for longer periods.

able to control their management, though the interference of its representatives should be limited strictly to the purpose of safeguarding the interests of the Bank. (e) Floating or promoting new industrial enterprises by placing the share capital on the market and underwriting a part or the whole of such issue. (f) Occasionally to extend liquid credits to companies against their stock-in-trade and trade bills. (g) Negotiating foreign loans, if necessary, for financing industries in the country.

All these operations fall within the sphere of Industrial Banks and must be carried on subject to the cautions and reservations referred to in the last section.

§ 35. The hoarding habit:—The habit of hoarding to which the Indian people are supposed to be subject in an unusual degree has long been the subject of comment among European economists. The description of India as a bottomless sink of precious metals is well known. With reference to the supposed insatiable hunger of India for gold and silver, it has been picturesquely observed that “ the precious metals are taken out of the earth by one coloured race and put back into it by another coloured race.” It is likewise said that gold once passed into general consumption in India is permanently lost to the rest of the world. Until recently, Europe has contemplated the steady absorption of the precious metals by India with amused wonderment not unmixed with satisfaction. If India had not swallowed up the gold and silver whose output had been enormously increased owing to the discoveries in recent times of new mines and the improvements in the methods of extraction, a great derangement in the economic life of the European countries would have been caused by a heavy rise in prices.* But latterly Europe has been showing distinct signs of alarm and consternation at the prospect of the Indian ‘ sink ’ continuing to perform its age-long function with habitual thoroughness. In 1924-25 when England and other countries of Europe were struggling to stabilise their currencies, India, entirely unmindful of the needs of Europe, added no less than 50 million pounds worth of gold to her hoards, which was perfectly shocking.

* See pp. 450-51 above.

The Indian hoards have been variously estimated. Probably the earliest estimate was that of H. D. Macleod, who was the first economist to get the Indian hoards on his brain. He tormented himself with the belief that the Indian hoards must be no less than £. 300 millions. Lord Curzon estimated the hoards at Rs. 825 crores. Arnold Wright writing in the Financial Review of Reviews, December 1916, estimated the amount of Indian hoards at £. 700 millions.* Mr. E. L. Price is inclined to accept a recent estimate of the American Trade Commissioner, who puts the hoarded wealth of India at £.1,000 millions. Mr. Francis Skrine thinks that this is very much of an underestimate†. So that with every fresh calculator, the calculations have proceeded in a regular *crescendo* movement.

In complaining about India's consumption of gold and silver, European writers have often seemed to impute a double dose of original sin to the Indian people and this apparent attempt "to fasten on India an exceptional and invidious responsibility for the consumption of gold"§ has provoked heated retorts. Some of these retorts are of the *tu quoque* variety. It is not India alone, it is pointed out, that is addicted to the consumption of gold. The United States absorbed nearly £. 500,000,000 worth of gold from 1916-1923.¶ Nobody, however, has called the United States a bottomless sink or a burial ground for the precious metals. A good deal of the gold in that country is no doubt concentrated in the central banking reserves, and if a similar use of it has not been possible in India, it is the faulty currency system (the gold exchange standard) which has been prevalent for a long time in India that is partly answerable for this. Those who bewail the hoards of India generally forget that part of the gold absorbed by India is used for industrial and domestic purposes, and, as Sir Stanley Reed remarks, "Every country in the world uses gold and silver for industrial and domestic purposes, and it induces a sense of angry injustice

* See B. R. Rau: op. cit. p. 214.

† See, Gubbay: op. cit., p. 23. and p. 38.

§ Memorandum of Sir Stanley Read to the Babington Smith Committee

¶ Wadia and Joshi : op, cit, pp. 388-89.

to find that the Indian demand for the precious metals for precisely the same purposes is perverted into senseless hoarding." Considering that India has a population amounting to about 19 per cent of the total population of the world, her annual (pre-War) consumption of about 20 per cent of the world's output of gold cannot be regarded as disproportionate or excessive.*

And when once it is granted that the Indian demand for gold and silver is not abnormal, all things considered, this acquits India of any particular responsibility for hindering the currency stabilisation in other countries. If India's legitimate demand for the precious metals is embarrassing to other countries, the latter must and will in course of time devise currency systems less dependent on gold than they have been in the past. It is also possible that India may in course of time take her share in any general world-wide movement for economising the available supply of gold, but she resents the suggestion that she is in a special sense responsible for its alleged scarcity at present.

All that has been said above aims at showing that the amount of hoards in India properly so called, is generally grossly exaggerated. It would, however, be flying in the face of facts to deny the existence of hoards altogether. A considerable amount of wealth, it must be admitted, is held by the people in the form of bullion and coin (and more rarely in the form currency notes). In passing it may be pointed out that although the aggregate amount thus accounted for may be considerable this is not a sign of wealth and prosperity. The hoards are held in endless, scattered, individually insignificant amounts and, moreover, being turned away from productive uses they are more properly regarded as a cause of poverty rather than an index of prosperity.

* It is sometimes urged in explanation and justification of the large imports of gold into India that they are after all due to India's favourable balance of trade caused by the keen demand for her goods on the part of her foreign customers. This contention, however, appears to us to be of little value. It must be remembered that India is as anxious to sell as the foreign countries are anxious to buy her goods and gold is sent to her in settlement of her trade balance because she prefers it to other commodities

It is a moot point whether it is permissible to regard gold and silver ornaments as constituting part of the hoards to the extent of their full value, though it is usual to assume them as such. But there seems to be no reason why jewellery worn for purposes of personal adornment should be looked upon as hoarding any more than gold used, let us say, for stopping teeth. Both are forms of consumption of wealth rather than of saving. It is no doubt true that when people in India turn gold and silver into ornaments they generally do so with the double object of personal adornment and holding wealth in store against a rainy day.* But it is all the same necessary to distinguish between the two motives and the precious metals can be regarded as hoards only in so far as they are intended to be stores of value.

Whether the Indian people are not inordinately fond of ornaments and jewellery and whether they do not invest a disproportionate amount of their earnings in them is a question which falls into the same category as a similar doleful inquiry which may be made, for example, with reference to the English workman asking whether he is not more fond of beer than is good for him and whether he would not benefit more by spending his money in other ways. Both are questions relating to intelligent and well ordered consumption. The spread of banking habits is no more a cure for misguided expenditure on ornaments than it is a cure for misguided expenditure on drink. The Indian peasant indeed often spends money on ornaments for himself and for his wife—ornaments too which, it is said, sometimes ulcerate more than they adorn—when perhaps he ought to spend the money on a mosquito-net, or more and better food. The use of gold and silver is in some cases forced by custom and plays an important part in social ceremonies sanctioned by religion and tradition. These are regrettable things but for remedying them we must rely on the development of a better sense of values as well as the softening of the rigour of social and religious custom through education and the progress of general enlightenment.

* The Babington Smith Committee also calls attention to the practical consideration that a woman, whether Hindu or Moslem, who possesses gold and silver ornaments, or coins converted into ornaments is entitled to hold them as her personal property.

But it must be clearly understood that this aspect of the matter is concerned with better or worse modes of consumption and expenditure and has nothing to do with hoarding proper the underlying idea of which is saving.

When all the allowances suggested by the considerations advanced above are made, there still remains a certain residuum for which the proper name, it must be admitted, is hoarding. Having granted that the evil does exist to some extent we must now proceed to analyse its causes. We have more than once referred to the faulty system of currency as a contributory cause. But the principal cause is found in the numerous invasions to which India was subjected in the past and the continued misrule and insecurity of life and property from which she suffered. The habit that was contracted in times of insecurity has continued to survive in times of well established peace and security, and the time has now come when the people must cure themselves of the wasteful habit. The obstacles in the path of reform are the illiteracy of the population and the absence of adequate banking facilities. The latest report of the Controllor of Currency comments with satisfaction on the welcome decline in the import of gold during the years 1926-27 and 1927-28, when the average net import of gold was only Rs. 18,75 lakhs as compared with an average of 28,15 lakhs for the five pre-War years. This together with the great success of recent Government loans * indicates a certain welcome increase in the investment habit, but only the fringe of the problem is as yet touched, and for its complete solution we must look to a widespread development of education and a much greater extension of banking facilities. The question of tempting the hoards into productive employment has latterly assumed a new importance. For though it may be true that the absence of a sound currency has encouraged the habit of hoarding, it is also true, on the other hand, that unless the hoards come out, it would be difficult for any currency system, however well devised, to function satisfactorily. For example, if hoarding persists, the control of currency and credit in the best possible way by the

* See Vol. I. p. 480.

currency authority would present insuperable difficulties. The extension of banking which is suggested as a cure for hoarding, is itself rendered difficult by hoarding. For how can banks carry on, if people will not put their money into them? But the other question is equally pertinent, viz., how can people put money into a bank, if there is no bank to put it into? It is thus a case of action and reaction, and the only remedy is to create as many credit institutions as possible and as great a variety of them as possible to suit the different needs and tastes of the people and leave education and continuous propaganda to do the rest.

§ 36. Fighting the Hoarding habit:—Various suggestions have been made for improving the present banking organisation and to fight the hoarding habit. Some of them taken individually may appear trifling, but the combined effect of all of them is bound to be very considerable. We shall mention some of these suggestions:

(I) The Post Office is a ubiquitous agency and it should be utilised to its utmost capacity for promoting the investment habit. The work it is already doing in this field has been noticed above and some improvements have been suggested. Other suggestions are that (a) the interest on Post Office five years cash certificates might be allowed to accrue after the first and each subsequent quarter instead of the fourth as at present; (b) the limit of the total amount of cash certificates in the case of joint holders, banks and co-operative societies may be raised from Rs.10,000 to Rs. 20,000; (c) the Savings Bank pass books should be bilingual, one of the languages being English, and the other, the principal vernacular of the part of the province in which the head office of the issue is situated. (II) The indigenous banking system should be made a part of a great national banking system starting with the village money-lender and ending with the State. For indicating the practical steps to this end, a comprehensive banking inquiry is necessary. A Resolution to this effect was moved in the Assembly in February 1927 by Mr. Haji asking for a commission with a majority of Indian members on it. The discussion on Mr. Haji's Resolution was resumed in August 1917 when Mr. K. C. Roy moved an amendment which was accepted. No action however, has yet been taken by Government.*

* See p. 508 above.

§ 37. Extension of Banking Facilities :—As regards the extension of more credit institutions, it is universally admitted that this is a crying need of the country. Compared to other civilised countries the number of banks in India is wholly inadequate to the real needs of the country. There are at present only some hundred head offices with 300 to 400 branch banks throughout the whole of India. In about 20 per cent of the towns with a population of more than 50,000 there are no banks at all; while in the case of towns with a population of 10,000 and over, the proportion without banking facilities rises to 75 per cent.* The following table† gives an interesting comparison of banking facilities in different countries.

Banking Offices in India and in Foreign Countries on 31st December 1924.

Name of Country	No. of Banking Offices	No. of Banking Offices per Million of Population	No. of Banking Offices per 2,700 sq. miles
United Kingdom	11,976	285	362
U. S. A.	30,000	256	20
Japan	7,465	92	80
Canada	4,883	448	3
India	596	2	1

While thus it is clearly necessary to multiply banking institutions, it is also necessary, as we have already hinted, to start diverse types of them. In this connection it must be mentioned that Joint-stock Banking of the ordinary kind may not always be found to be suitable for Indian conditions. Other more suitable models which might be tried are furnished by the popular Co-operative Banks in Germany and Italy. The popular Banks in Italy keep the shares as low as possible in order to encourage the small investor. Also the dividend is limited sometimes by law and sometimes by custom. Special terms are

* See India in 1924-25, p. 146.

† Presidential Address of Principal M. L. Tannan, Indian Economic Conference, Calcutta, 1927.

offered to poor investors as an encouragement to saving and loans are advanced at low rates. Loans are also given on personal credit for objects approved of by the banks. Institutions of this kind are likely to flourish in India more than the usual kind of Joint-Stock Banks.*

§ 37. Institute of Bankers for India:—As we have already seen, one of the reasons for the Bank failures in 1913-14 was the generally prevalent ignorance of banking in India. The creation of an Institute of Bankers has been advocated in many quarters in order to remove the defect. The question has received special attention during recent years, and Sir Basil Blackett announced in the Assembly in March 1927 in connection with Mr. Haji's Resolution on an enquiry into Indian banking, that the proposal for an Indian Institute of Bankers was about to materialise and that the British Institute of Bankers had been giving advice and assistance in the matter. Accordingly the Indian Institute of Bankers was registered at Bombay under the Indian Companies Act, on the 20th April 1928. The main objects of the Institute are:—(1) to support and protect the character, status and interests of persons engaged in or connected with the business of banking generally and especially in India, and consider all questions affecting them; (2) to encourage the study of the theory of banking and for that purpose to institute a scheme of examinations and grant of certificates, scholarships and prizes; (3) to spread information on banking and kindred subjects by means of lectures, discussions, periodicals, books, correspondence with public bodies or individuals, etc.; (4) to collect and circulate statistics and other information relating to the subject of banking in India,† A syllabus has already been issued of the Associate Examination of the Institute which will be held in the spring of each year.

§ 38. The question of the Reserve Bank—We shall now discuss the question of the Reserve Bank which is proclaimed to be

* See Guabby, op. cit. pp. 29-32.

† See Memorandum and Articles of Association of the Indian Institute of Bankers (1928).

the crowning glory of the new currency and banking system in India. We have already indicated the main functions to be assigned to the new Bank, which is expected among other things, to be a banker's bank and to unify the control over the banking and currency reserves of the country. The Reserve Bank is calculated to help India "to move forward towards that financial and economic development with the granting of additional financial and banking facilities for Indian agriculture, Indian commerce, and Indian industry, which has been the theme of one Commission and Committee after another. We shall see the development of a discount market and acceptance business, of increased facilities for the marketing of produce and, in short, a gradual mobilisation of India's immense potential capital for the development of India's own resources."† The general case for a Central Bank has already been stated.§ Such a Bank has been widely desired in India not only on account of the improvement in banking and currency machinery which it promises, but also because" the growing political consciousness of the country has led to the search for all national emblems, amongst which a central State Bank is one."¶

§ 39. Case for a brand-new creation:—The Imperial Bank was intended to serve as a State Bank but we have already seen reasons for denying that it actually occupies any such position. It performs one or two functions of a true Central Bank and there has been much debate on the question whether it would not be desirable to turn it into a proper Central Bank, but the objections to this step are various and overwhelming. In the first place the Imperial Bank is a private corporation frankly out to earn money. The large number of branches which it has been compelled to start has forced it to become a commercial bank. Commercial banking however is incompatible with the position of a real Central Bank. It is also unfair that the Imperial Bank, with advantages even greater than at present which it would enjoy as a Central Bank by holding the reserves of other banks and the

* See page 433 above.

† Sir Basil Blackett's speech introducing the Reserve Bank Bill.

§ See § 21 above.

¶ Pat Lovett: *The Mirror of Investment*, 1927, p. 19.

balances of Government, should be allowed to enter into competition with other banks not endowed with these privileges. The functions of a true banker's bank are protective and not competitive. Moreover, a large number of branches is not a help but a positive impediment to a Bank of Issue, which wants branches only at a few important places. If the Imperial Bank were to be converted into a Central Bank its charter would have to be radically altered so as to deprive it of its present functions as a commercial bank. The Hilton Young Commission also argued that the Imperial Bank had been playing a very useful role in the credit organisation of the country, especially since 1920, by establishing branches in various parts of the country and that it would be unwise to check this useful career by restricting the functions of the Bank to those of a central bank. On the contrary it would be desirable to free the Imperial Bank altogether from the restrictions at present imposed upon it—restrictions which clearly have their origin in the hybrid character of the functions originally assigned to it. With the withdrawal of its central banking functions it would be freer and more competent to perform its important task of spreading banking facilities in India. The Commission, therefore, favour the establishment of a separate and entirely new Central Bank and propose that the Imperial Bank should carry on important agency work for the Reserve Bank. This view has been generally endorsed in the country. We have already stated that the Imperial Bank has not succeeded in winning popular esteem and has never been held to be remarkable for any broad national outlook essential for a Central Bank, and public opinion on the whole is strongly against its metamorphosis into a Reserve Bank.

§ 40. The Hilton Young Commission's Proposals.—The Hilton Young Commission propose that the Reserve Bank should be a private shareholder's bank. The constitution which they propose for the Reserve Bank is on the same lines as that of the Imperial Bank and they consider that, having regard to the large area of the country and its diversity of local conditions, the system of local head offices in the chief business centres managed by Local Boards elected by shareholders registered in the respective branch registers would be the most appropriate. The Central as well as

the Local Boards should be independent of Government and free from all political pressure, and a predominant majority of their members should derive their mandate from the shareholders of the Bank by election, only a small minority on the Board being nominated by Government. The presence of Government nominees is needed in view of Government's experience in currency matters and the great importance of their banking and remittance business. To eliminate the danger of political pressure, however, the charter of the Bank should direct that no person shall be appointed President, or Vice-President of a Local Board, or shall be nominated a member of the Central Board if he is a member of the Governor-General's Council, the Council of State, the Legislative Assembly, or any of the Provincial Executive or Legislative Councils.

Detailed recommendations are made about the note issue, composition and location of reserves etc. some of which have already been mentioned.* So far as the gold and gold security reserve against notes is concerned, the Commission reject the model set up by the English Bank Charter Act of 1844 as too rigid especially for Indian conditions in view of the poor development of the cheque currency.

The Commission, therefore, recommend the Proportional Reserve system ‡ under which the notes in active circulation are secured by a minimum percentage of gold or gold securities laid down by statute, which may be transgressed for a temporary period on the payment of a tax on the deficiency and with the consent of the Government. The Proportional system permits of a far wider expansion and contraction of the circulation than the fixed fiduciary reserve system. There is no greater scope for inflation under this system than under the English system. For, under the latter system also, undue expansion of credit can take place through the inflation of the cheque currency. Both systems, in fact, require prudence in the management of currency and credit.

The Commission further proposed that the Bank Act should

* See p. p. 413-15 above.

‡ See p. 413 above.

also include provisions compelling every bank or banker transacting business in India to establish and maintain minimum reserve balances with the Reserve Bank equal to 10 per cent of its or his demand liabilities, and 3 per cent of its or his time liabilities.

§ 41. State Bank vs. Shareholder's Bank :—In January 1927 Government introduced a Bill framed on these lines. The Bill proposed a Shareholder's Bank with a commercial directorate and a new agreement with the Imperial Bank freeing it from some of its old restrictions. The Bill was referred to a Select Committee in which a sharp difference of opinion showed itself on the fundamental point as to whether the Reserve Bank should be a State Bank or a Shareholder's Bank and as to the constitution of the Central Board. So far as it is a matter of principle, the widely accepted view is that a Shareholder's Bank is preferable and that a Central Bank should be regarded more as a large public trust than a department of state.* It is true that state control is necessary to some extent, because the state has its own interests to protect and moreover must be in a position to prevent the Bank from degenerating into a purely dividend-hunting concern and ceasing to be a true national institution. However, it is better to start by making the Bank an independent organisation keeping for the state such specific and limited powers as may be essential rather than establish a State Bank and then devise machinery to make the Bank independent of government in some measure. The very fact of state ownership affords facile pretexts for undue interference on the part of the Government. With reference to the proposal that members of the Legislature in India should select some members of the directorate of the Reserve Bank and should themselves be eligible for becoming directors, it is objected that this would mean the introduction of "political pressure in its least desirable form—in a party form as well as personal form. For, the panel which is to be put forward by the Assembly,.....would naturally include men chiefly from the dominating party of the day" and "through personal and direct

* See Kisch and Elkin : op. cit. p. 17.

action of the party members thus sent on to the Board of Directors, the eddies of political feeling and antagonism would act directly on the policy of the Bank." Such a system would also impose additional heavy work on the Legislature which is already burdened with more work than it can quite cope with.* The fear of the predominance of large capitalists, especially foreign capitalists, it is pointed out, could be met by the allocation of the Bank's shares by preference to small subscribers and to persons of Indian domicile. Another objection to a State Bank is that it would tend to be an effete institution excessively dependent on a lead from Government in everything.

The Majority of the Select Committee, however, objected to a shareholder's Bank on the following grounds:—That a Reserve Bank in charge of currency and credit ought in the fitness of things be made responsible to the Legislature; that only a State Bank would inspire confidence among the people in India; that a Reserve Bank does not require much capital and therefore there is no necessity of a body of shareholders, The Select Committee attached much importance to the argument referred to above, viz., that a shareholder's Bank is likely to involve domination of the Bank by large capitalists in the big cities.‡

Regarding the composition of the Directorate, the Majority proposed that there should be a Board consisting of 15 governors and one officer, with a majority of Indian elected members including three members elected by the elected members of the Central Legislature and another three similarly elected to represent agriculture by the Provincial Legislatures. The two directors to be appointed by the Governor-General-in-Council must be Indians as also the Governor and the Deputy-Governor of the Bank. Two directors were to be elected by the Associated Chambers of Commerce and two by the Federation of the Indian Chambers; one director was to be elected by the Provincial Co-operative Banks. The officer of the Government was to be appointed by the Governor-General in-Council and was not to be entitled to vote.

* See Coyajee : *The Reserve Bank of India*, p. 18.

‡ See Times of India Year Book, 1928, p. 318.

§ 43. Fate of proposed legislation:—The Bill as amended by the Select Committee was taken up by the Assembly in the Simla Session in August 1927. The scheme of the State Bank was incorporated in the Bill, but agreement could not be reached on the question of the directorate. Government were defeated on their proposal to disqualify a member of the Legislature from being a Director of the Bank and the House was strongly against the proposal of the Government to delete the recommendation of the Select Committee that the Governor and the Deputy Governor must be Indians. Sir Basil Blackett accepted in principle the State Bank scheme and the amendment of Mr. S. Iyengar that the six directors instead of being elected by the Legislatures, should be elected by certain electoral colleges and that there should be an Indian majority on the Board. Complete agreement not having been reached, Sir Basil brought forward a fresh scheme which appeared to have a fair chance of passing in the Assembly. But the Finance Member sprang a surprise on the Assembly by announcing on the 8th of September that Government did not wish to proceed with the Bill during the session as there was no agreement on the question of the Directorate. This aroused considerable criticism and it was alleged that the Government of India were acting under instructions from the Secretary of State who apparently objected to the drastic changes in the original scheme.

After conferring with the Secretary of State the Government of India decided to drop the old Bill and published a new Bill in January 1928 prior to its introduction in the Assembly. The new Bill abandons the State Bank idea and reverts to the Shareholder's Bank. It provides for a broadbased distribution of the share capital by the issue of shares of one hundred rupees each, limitation of the amount to be subscribed, allotment of specified shares to Bombay, branches at Calcutta, Madras, Rangoon and Delhi, and adoption of certain qualifications for shareholders so as to ensure a predominant share of the capital to persons and companies domiciled in India or registered by Acts of Parliament, and scheduled banks which are required to maintain certain minimum reserves with the Bank. Members of the Legislatures are prohibited from being Directors.

The following composition is proposed for the Central Board. (i) A Governor and Deputy Governor to be nominated by the Governor-General-in-Council on the recommendation, if any, of the Board; (ii) four Directors to be nominated by the same authority; (iii) two to be elected by the Associated Chamber of Commerce; (iv) two by the Federation of the Indian Chambers of Commerce (v) one to represent agriculture elected by the Provincial Co-operative Banks; (vi) eleven Directors to be elected by the shareholders on the various registers, (vii) one officer to be nominated by the Governor-General-in-Council. The shareholders are first to elect, once in five years, a certain number of delegates who will elect the Directors.

The new Bill was ill-fated, and spectacular developments followed when in the Delhi session (1928) of the Assembly the President refused to call upon the Finance Member to move his Bill on the ground that he could not do so under rules of parliamentary procedure until the old Bill was formally withdrawn or lapsed. Government thereupon decided to proceed with the old Bill which they had abruptly postponed in September 1927. With this decision, all the old troubles revived and the opposition was too strong for the Government to be able to push through their proposals regarding the constitution of the Board. Government therefore announced that they had no intention of proceeding with the Bill in view of the temper displayed by the House which seemed to preclude any sort of a workable compromise. The Reserve Bank and the financial *Swaraj* it was going to bring are thus postponed *sine die*.

This is unfortunate, because the Reserve Bank constitutes the most vital part of the scheme for the modernisation of India's financial machinery. It is to be hoped that a spirit of mutual concession will prevail and a way will soon be found out of the impasse.

CHAPTER XII

FINANCE AND TAXATION.

§ 1. Introductory observations:—Before plunging in *medias res*, we shall make a few general introductory remarks on Indian finance and taxation. Indian finance has in recent years undergone remarkable—almost revolutionary—changes many of which are directly or indirectly traceable to the War. Before the War there was only one budget for the whole of India, and the Provincial Governments had no independent powers of taxations. The Central Government was the only taxing authority (unless we also take into account the very limited powers of taxation enjoyed by the Local Bodies). After the War there has been a practically complete separation of Provincial from Central finance. A considerable change has also been going on for the last half a century or so in the relative position of the different sources of revenue. In the course of this period the land revenue has lost its old overshadowing importance and other sources of revenue have come into greater prominence. About forty years ago land revenue contributed 53 per cent of the total receipts of Government. It now contributes only about 20 per cent. During the same period the income from customs has gone up from less than 3 per cent to about 24 per cent and that from the Income Tax from just over $1\frac{1}{4}$ per cent to $12\frac{1}{2}$ per cent.* The financial system of India has been recently coming more and more into line with other modern systems as shown by the increasing variety of her taxes and the growing reliance on direct taxes like the income tax. Another great change has been with regard to the position of railways in Indian finance and we have already noticed their evolution from blood-sucker to milch-cow. Opium which not long ago used to make a brave show on the

* Taxation Enquiry Committee's Report.

revenue side of the budget and was second in importance only to land revenue has suffered almost a total eclipse as the result of India's great essay in philanthropic finance.

§ 2. Classification of Indian Revenues:—Indian Revenues can be classified according to the authorities charged with the power of levying the taxes from which they are derived, as Provincial, Central and Local (Revenues of Municipalities and Local Boards). Another classification which is as good as any other is the following.*

I. *Land Revenue*:—In Chapter XII, Vol. I. we have already dealt with the question whether land revenue is a rent or a tax, and we saw that there are more reasons for calling it a tax than there are for calling it a rent. If this view is accepted land revenue would be a direct tax like income tax. But since in this controversy absolute certitude is unattainable, it would perhaps be better to cut the Gordian knot by regarding land revenue as a class by itself. II. *Taxation Revenue*:—Under this head we have the usual sub-classes of direct taxes and indirect taxes. The income tax and other assessed taxes and the land cesses included under Provincial Rates are instances of the former. The salt tax, excise, customs, stamps and registration are the principal indirect taxes in India. III. *Public Monopolies*:—This head includes the revenue from forests and opium. IV. *Commercial services*:—Railways, irrigation, public works, Posts and Telegraphs. V. *Miscellaneous receipts*:—e. g. tributes, departmental receipts, etc. VI. Interest on loans given to the Local Bodies, Provincial Governments and Indian States.

We shall now discuss some of the heads of revenue§ shown in the following Table:—

* See K. T. Shah: *Sixty years of Indian Finance*; pp. 214-15.

§ The question of the division of revenue between the Central and Provincial Governments is discussed later on.

The Revenues of India (Central and Provincial) 1925-26.

(In thousands of rupees.)

Principal Heads of revenue :-	Central	Provin- cial	Principal Heads of revenue :-	Central	Provin- cial
Customs	47,77,95	.....	Railways (net receipts)	34,40,12	3,27
Taxes on in- come	15,85,93	26,10	Irrigation (net receipts)	12,03	7,48,15
Salt	6,32,96	.....	Posts & Tele- graphs	86,35	.....
Opium	4,14,99	.....	Interest	4,21,95	2,34,07
Land revenue	38,52	35,16,77	Civil Admini- stration	89,97	3,58,82
Excise	42,20	19,47,65	Currency & Mint	4,63,89	.....
Stamps	27,14	13,38,45	Civil Works	12,85	68,18
Forests	18,74	5,80,44	Miscellane- ous	54,17	2,03,70
Registration	1,68	1,43,70	Military re- ceipts	4,39,51	.....
Tributes from Indian States	84,29	.....	Contributions assigned to the Central Government by Provincial Govts.	6,08,40	-6,08,40
Scheduled taxes	.....	35,71	Extraordina- ry items	63,57	1,55,12
Total ...	76,24,44	75,88,25	Total revenue	1,33,17,30	87,51,20

§ 3. Opium:—As already hinted above, opium was until recently a very considerable source of revenue, and the occasional wind-falls from this head were at one time notorious. With regard to the administrative aspect of opium revenue the method of production and sale under Government monopoly was adopted in preference to heavy export duties, as being more satisfactory from the revenue point of view and as obviating the possibility of smuggling.

The revenue from opium is derived from three main sources:—
(i) The monopoly profits of the sale of opium manufactured in Government factories and intended for export to foreign countries;
(ii) Income from the export duty levied on the purchase of opium sent out from the Native States of Rajputana and Central India; and (iii) profits of monopoly in the form of license fees or vendor's fees derived from the internal consumption of opium in British India. This revenue is credited to or shown under the revenue from excise and that from the first two sources under opium proper.

In 1907, under pressure from Whitehall, the Government of India entered into an agreement with China, and undertook to stop the export of Indian opium to China in ten years by a progressive reduction every year. China was to restrict her own production of opium and curtail her imports from elsewhere. The period of ten years was shortened by a further agreement in 1911, and since 1914, there have been no sales on Government account for export to China. The curtailment of exports to China was effected at the dictation of the Secretary of State who in his turn was influenced by strong agitation in England in favour of the suppression of opium traffic with China. It was said that in this manner British righteousness was satisfied at the cost of Indian revenues. It was also complained that China herself had failed to fulfil her part of the agreement and had been unable to decrease her own production of opium. All the same India ought to be satisfied that she has done her duty by China and ought to cease regretting the loss of revenue, as she has almost succeeded in doing. The loss of revenue from the curtailment of the export to China was not felt immediately on account of the rise in price of the opium sold. But at present, the revenue from opium is very much lower than formerly, being about Rs. 3 crores as contrasted with the annual average of about 8 crores during the three years preceding 1913. It was announced by Lord Reading in Feb. 1926 that Government intended to abolish all exports of opium in future except for strictly medicinal purposes. We may therefore expect a further fall in the revenue, which will be emphasised by Government's policy of strictly regulating internal consumption of the noxious

drug which is still high according to the standard laid down by the League of Nations. With effect from April 1926, opium is now exported under the system of direct sales to foreign and Colonial Governments, the old system of auction sales in Calcutta having been discontinued. An import certificate is required in each case from the government of the country of import as prescribed by the League of Nations, before exports are permitted.

§ 4. Salt:—The salt revenue was inherited by the British Government from its predecessors along with a large number of transit dues which were abolished in 1843 and the salt duty was at the same time consolidated and raised. Before 1882 the rate of the duty varied from province to province. In that year the rate was made uniform at Rs. 2 per maund but was raised to Rs. 2-8-0 in 1888 in the period of falling exchange. It continued at that level down to 1903 when easier finances permitted its being lowered to Rs. 2-4-0. It was further reduced to Rs 1-8-0 in 1905 and to Re 1-0-0 in 1907, at which level it continued till 1916, when financial stringency led to an increase in the duty to Rs. 1-4-0. In the budget of 1923, Government's proposal to raise the duty to Rs. 2-8-0 was rejected by the Assembly but was carried through by Certification by the Governor-General. In 1924, however, the Assembly exercised the option given to it by the Government in favour of reducing the salt tax to Rs 1-4-0 per maund as an alternative to reductions in the Provincial Contributions. This is the rate at the present moment.

There are two principal methods of levying the duty on the salt produced in the country. (i) The Government either manufactures the salt or obtains a monopoly of the supply, requiring private manufacturers to sell it to Government only. It is then sold by Government on payment of the duty. (2) Secondly, as in Madras, the Government levies an excise duty and allows the manufacturer to sell the salt to private traders or the consumers. Government factories are in some cases leased to private individuals who manufacture and dispose of salt under a license from Government.

§ 5. Criticism of the Salt tax:—The salt duty although it is ancient is one of the most unpopular taxes in India. It has been justified on the ground that it affords the only means in a country like India of reaching the masses by direct taxation. It is an accepted maxim of statecraft that every citizen should contribute something, however little, to the expenditure of the State. This will help him to develop a sense of responsibility and prevent him from supporting wholesale and costly changes in a reckless fashion. To this however a reply may be made that another obvious way for Government to satisfy their political conscience is frankly to accept the position that the land revenue which practically everybody pays in India is a direct tax.* In the case of those who do not pay the land revenue it is generally a safe inference that they are so utterly indigent that the idea of taxing them should be given up in spite of any political principle to the contrary. The principal objection to the Salt Tax is that it is a tax on a necessary of life and a restriction in its consumption has an undesirable effect on the physique of the people. The fact that successive reductions in the Salt Tax from 1903 onward have been followed by a considerable increase of consumption suggests that the tax had been kept at an unwisely high level before. It is a regressive tax since it presses more heavily on the poor than on the rich; for a comparatively larger proportion of their income is spent by the poor on salt than by the rich. The Salt Tax is often defended on the ground that it is an old tax and that an old tax is no tax in the sense that from sheer habit people cease to think of it as a hardship. Essentially, however, the tax is undesirable and, though for practical reasons it may be impossible to abolish it immediately, this should be definitely recognised as the goal of public policy and steady approaches should be made towards it. So long as the tax cannot be dispensed with, it should at least be maintained at as low a pitch as possible.† The existing machinery for collection makes it possible to secure additional revenue

* cf. K. T. Shah : *Sixty Years of Indian Finance* p. 254.

† Dr. Paranjpye suggests 8 annas per maund as the normal rate of the tax. See Taxation Enquiry Committee's Report para 168.

from this source with comparative ease, but an increase should not be thought of except in case of grave emergency and should last only during such emergency.

§ 6. History of the Income Tax:—The Income Tax has a very long and chequered history. A general income tax was first levied to meet the financial burdens of the Mutiny, for five years, at the end of which it ceased to operate in 1865. In 1867 another Act was passed imposing a license tax on professions and trades excluding agriculture, and this tax continued to be levied till the end of 1872-73. No further taxation was imposed till 1877, when a license tax was levied on traders and artisans to meet a portion of the Famine Insurance Grant, and Acts were passed in 1878 for this purpose for the United Provinces, the Punjab, Madras, Bengal and Bombay. These Acts remained in force until 1886. The license tax of 1878 was, however, converted into a general income tax by the Income Tax Act of 1886 applying to all India. Under this Act, all sources of non-agricultural income were taxed and were divided for this purpose into four classes. (1) Salaries and pensions; (2) profits of companies; (3) interest on securities; and (4) other sources. On all annual incomes between Rs. 500 and Rs. 2,000 derived from salaries and interest on securities, a tax of 4 pies in the rupee was levied; while on incomes over Rs. 2,000 and on all profits of companies the tax was 5 pies, there being no further graduation of the tax. Similar incomes derived from other sources were taxed at practically the same rates, charities and religious endowments being exempted. In 1903, the favourable condition of the finances permitted exemption from the tax of incomes between 500 and 1,000.

§ 7. Changes in the income tax during and since the War:—

1916.—Scale of progression introduced in the ordinary income-tax.

1917.—A super-tax in addition to the ordinary income tax on a progressive scale was introduced.

1918.—The machinery of income-tax was amended and improved.

1919.—(A) The free minimum income was raised from Rs.1,000 to Rs. 2,000 a year. (B) Excess war profits-tax was levied for a year on incomes in excess of Rs. 30,000—agricultural incomes, incomes of professional classes and public servants being exempted.*

1920.—Abolition of the excess war-profits tax. Amendment of the Super-tax Act in regard to profits of companies and registered firms.

1921.—The scale of progression both in the ordinary income-tax and the super-tax revised and raised.

1922.—A further revision of both the kinds of taxes in an upward direction.

The rates of ordinary income tax as at present (first introduced in 1922).

Incomes less than Rs. 2,000 exempted;				
Incomes between Rs. 2,000 & 5,000 pay 5 pies in the Re.				
"	"	5,000 & 10,000	" 6	"
"	"	10,000 & 20,000	" 9	"
"	"	20,000 & 30,000	" 12	"
"	"	30,000 & 40,000	" 15	"
"	"	40,000 and over	" 18	"

In the case of every company and firm, whatever the total income : 18 pies per rupee.

These are the rates of the ordinary income tax. In 1916 the highest rate was 12 pies on Rs. 25,000 and above. In 1921, it was 16 pies on Rs. 40,000 and above. In 1922 the maximum rate was raised to 18 pies on Rs. 40,000 and above.

Super-tax indicating the present rates (introduced in 1922).

In the case of a Hindu undivided family, in respect of the first Rs. 75,000 of the taxable income, no super-tax is levied; on the next Rs. 25,000, the super-tax is one anna in the rupee.

* Government proposed to take half of the excess profits defined as the difference between the profits returned in 1918-19 and the average of the profits returned in the two pre-war years and the first two years of the war. The tax was paid by incomes in excess of Rs.30,000.

In all the other cases, in respect of the first Rs. 50,000 of income, no super-tax is levied. But on the next Rs. 50,000, it is one anna per rupee. Then the further regulations are common to all incomes as follows :—

On all incomes between 1 lakh and 1½ lakhs	As.	1½ per rupee
On every rupee of the next Rs. 50,000	„	2 „
„ „ 50,000	„	2½ „
„ „ 50,000	„	3 „
„ „ 50,000	„	3½ „
„ „ 50,000	„	4 „
„ „ 50,000	„	4½ „
„ „ 50,000	„	5 „
„ „ 50,000	„	5 „
For every rupee of the remainder of the excess	„	6 „

These last (i. e. incomes between 5½ lakhs and above) would pay the ordinary income-tax at the highest rate of the ordinary income-tax at 1½ annas in the rupee and super-tax at six annas in the rupee, so that they pay a total income-tax of just less than 50 per cent. (7½ As per rupee).

The highest rate in 1917, when the super-tax was first introduced, was 3 annas in the rupee on incomes of 2½ lakhs and above. In 1921 it was 4 annas in the rupee, on all incomes of Rs 3½ lakhs and above. In 1922, it was raised to the existing rate of 6 annas in the rupee on income of 5½ lakhs and over.

Before the amending Act of 1920 the incomes of companies and registered firms paid the same super-tax rates on their undivided profits as the other incomes. But by that Act a new super-tax at the flat rate of one anna in the rupee on the whole undivided income of the companies and firms in excess of Rs. 50,000 was levied. This change was effected as the old system gave an incentive to companies to distribute more in dividends than was warranted by their real financial position and penalised those companies which endeavoured to strengthen their reserves. In the year 1922, the flat rate was raised to 1½ annas in the rupee whatever the total income in excess of Rs. 50,000. The present rate is 1 anna in the rupee.

§ 8. History of the Customs Tariff:*(A) *Pre-War Import Tariff*:- Until quite recently, the Indian tariff had been on a scrupulously conscientious free trade basis. This involved very moderate import duties. Before the Mutiny there was an import duty of 5 per cent on finished goods and $3\frac{1}{2}$ per cent on raw produce. Goods imported in foreign ships had to pay double the ordinary scale of duties till 1848. After that date the nationality of the shipping was ignored, though differential duties continued to be levied up to 1859 in accordance with the nationality of the goods, being double the ordinary rate on non-British goods. On account of the financial stringency which followed the Mutiny, this distinction was abolished and the general rate was raised to 10 per cent. It was reduced to $7\frac{1}{2}$ per cent in 1864 and 5 per cent in 1875. And eventually in 1882 all customs duties were abolished under pressure from the British Government inspired by the Manchester interest and in spite of the opposition of the then Viceroy, Lord Northbrook.

Between 1882 and 1894 there were thus practically no import duties. But in 1894 owing to financial stringency a 5 per cent *ad valorem* general import duty was imposed, cotton yarn and piece-goods and certain other goods being excluded from the operation of the tariff.

Between 1899 and 1904, certain countervailing duties were imposed on bounty-fed sugar coming from Germany, Austria, Denmark and so forth. These were subsequently removed, the last duty of the kind being cancelled in 1912. Their only effect was to divert the import trade in sugar from Germany and Austria to other countries like Mauritius and Java where the system of bounties did not exist.

The only other important changes in the pre-War period in the import tariff were effected in 1910-11, when to compensate for the loss of the revenue from opium and to meet additional expenditure, higher import duties were levied on silver bullion

† Under the heading "customs" is included not only the revenue from the import and export duties but also the excise duty on cotton manufactures and petroleum.

or coin, and petroleum. We have already seen that the former was cancelled as recommended by the Smith Committee.

At the end of 1894 it was decided to levy a 5 per cent import duty on cotton fabrics and yarn, but to propitiate Manchester, a duty of 5 per cent was levied on yarns of 20 counts and above produced in Indian mills. This excise on yarn did not give full satisfaction to Lancashire, and therefore in 1896, the import duty on cotton piece-goods was lowered to $3\frac{1}{2}$ per cent and an excise duty at the same rate was placed on all Indian mill-woven cloth; cotton yarn, whether foreign or local, being altogether exempted from any duty.

This measure was bitterly resented in India. The excise duty seemed to injure India without benefiting Manchester. As was pointed out by Sir James Westland, of the cotton manufactures of India, 94 per cent was outside the range of any competition with Manchester, being of coarser qualities (24s and under). Manchester had an absolute monopoly of the finer qualities of goods and the bulk of its trade consisted of piecegoods of counts about 30 or somewhat finer, and India could only produce goods of counts 26s or over in small quantities and under difficulties. Lastly, the reduction of the import duty from 5 to $3\frac{1}{2}$ per cent would benefit the richer consumers of foreign cloth, while the home excise of $3\frac{1}{2}$ per cent would affect the poor consumer adversely. The case against the excise duty appeared unanswerable. But, as was wittily remarked by an Indian member of the Imperial Legislative Council, so long as Lancashire sent sixty members to Westminster, the British government would always have sixty good reasons for maintaining the duty, and thus the duty remained in spite of continued opposition on the part of the people till it was finally abandoned in 1926.

(B) *Export Tariff*:—The history of the export tariff in the pre-War period can be more briefly disposed of.

Until 1860, export duties were an integral feature of the early tariff policy and were levied generally at the rate of 3 per cent *ad valorem* on practically all exports for revenue purposes. Though the duties were low and solely for revenue purposes, the principle of export duties was regarded as economically unsound as likely to do injury to the export trade by encouraging foreign

competition. Accordingly a consistent policy of abolition was pursued from 1860 to 1880, so that at the latter date only the export duty on rice was allowed to remain. In 1903, a trifling duty was levied at the request of the Indian tea industry on the export of tea.*

§ 9. War and post-war Customs Tariff:—Extensive changes in the customs tariff were introduced during the war and the post-war period which are briefly summarised below.

(A) *Import Duties* :— The general *ad valorem* duty was raised to $7\frac{1}{2}$ per cent in 1916-17 (cotton piecegoods not being raised to $7\frac{1}{2}$ per cent till 1917-18); to 11 per cent in 1921-22 (including cotton piecegoods); and to 15 per cent in 1922-23 (cotton goods remaining at 11 per cent). Railway materials were taxed at $2\frac{1}{2}$ per cent in 1916-17 and the tax was raised to 10 per cent in 1922-23. Iron and Steel were raised from 1 per cent to $2\frac{1}{2}$ per cent in 1916-17, and to 10 per cent in 1922-23. Sugar was increased from 5 to 10 per cent in 1916-17, and from 15 per cent to 25 per cent in 1922-23. Machinery and stores for cotton-spinning and weaving were taxed at $2\frac{1}{2}$ per cent in 1921-22, but exempted later on (see pp. 61-62 above). A high specific duty on matches at 12 annas per gross boxes was imposed in 1921-22 instead of the $7\frac{1}{2}$ per cent *ad valorem* duty. This duty was doubled in 1922-23. Luxury goods like motor cars, cinema films, watches, silk piecegoods etc. were raised from $7\frac{1}{2}$ per cent to 20 per cent in 1921-22 and 30 per cent in 1922-23. The duty on motor cars was reduced from 30 to 20 per cent and that on tyres was reduced from 30 to 15 per cent in 1927-28, in accordance with the recommendation of the Taxation Enquiry Committee, which stressed the importance of encouraging motor transport in India. The reduction in the duty leaves a wider margin for provincial taxation on users of motor cars for the improvement and development of the provincial systems of road communication. The tobacco duties were raised to 75 per cent *ad valorem* for cigars and cigarettes in 1922-23. In 1923 unmanufactured tobacco was raised from Rs. 1-8 per lb. A 5 per cent duty was imposed on foreign cotton yarn

* See Vol I p. 207.

which had been free since 1893. Recent changes regarding foreign cotton yarn have already been noticed (see p. 62 above). A duty of one anna per gallon was put upon kerosene and petroleum, with a corresponding excise duty on the home products. The duty on imported liquors was increased in 1921-22 and again in 1922-23.

(B) *Export Duties*:—In 1916-17, two new export duties were levied on tea and jute. In the case of tea the export duty was fixed at Rs. 1-8-0. This duty was abolished in 1927-28, but its abolition was accompanied by an increase in the income-tax assessment on the profits on the Tea industry.* In the case of jute, the export duty was fixed at Rs. 2-4-0 per bale of 400 lbs. being approximately equivalent to an *ad valorem* duty of 5 per cent; manufactured jute was charged at the rate of Rs. 10 per ton on sacking, and Rs. 16 per ton on Hessians. In 1917-18, the export duties on jutes were doubled. In October 1919, a 15 per cent *ad valorem* duty was levied on raw hides and skins as a measure of protection to the Indian tanning industry.†

The War and post-War years have thus witnessed the most striking changes in the customs tariff. The needs of war finance and the post-war financial deficits have called into existence a marked tendency of greater and greater reliance on customs duties. The growth of revenue (gross) from customs from 1914 to 1928 is shown on the next page.

All these changes effected under the stress of financial stringency have changed the nature of the customs duties and the position occupied by them in the Indian fiscal system. A high general duty, wide breaches in the principle of uniformity, a curtailed free list, special taxes on articles of luxury and on sugar, and lastly, the imposition of new export duties are among the

* By the Income Tax Act of 1927, the Tea companies were assessed to 50 p. c. (later reduced to 40 p. c.) of their total income, subject to the proviso that, where there is a market for green tea and the non-agricultural profits can be exactly ascertained, income tax should be assessed on the total of such non-agricultural profits. Till this Act was passed, only 25 p. c. of the total profits were assessed to the income, the rest being regarded as agricultural income and therefore exempt from the Income Tax.

† See p. 45 (footnote) and pp. 76-77 above.

Growth of Customs Revenue.

Year	Crores of Rupees	Year	Crores of Rupees
1213-14	11.13	1924-25	45.75
1918-19	18.18	1925-26	47.77
1921-22	34.60	1926-27	47.38
1923-24	39.69	1927-28	48.63
		1928-29	50.18 (Budget Estimates).

more important features of the new tariff as contrasted with the pre-war tariff.

These changes in the tariff (except as regards the export duty on raw hides and skins) were governed by revenue considerations only. Some of the duties were, however, so high as to produce a definitely protective effect. We have already noted how this strengthened the case for a properly thought out system of protection in place of the haphazard protection which had come to be unwittingly introduced. Since the passing of the Steel Protection Act of 1924, several frankly protectionist duties have been imposed. The work of the Tariff Board after the initiation of the policy of protection has already been noticed in Chapter III with reference to steel, paper, printer's ink, textiles, machinery, and manufacture of matches.

As regards the incidence of the increased customs duties, the Taxation Enquiry Committee* found that there was an increase of customs revenue from 430 lakhs in 1913-14 to 1,746 lakhs in 1924-25 i. e. 307 per cent in the case of articles of direct consumption consumed by the population as a whole, while in the case of articles mainly consumed by the richer classes the increase was from 400 lakhs to 1,416 lakhs or by 254 per cent. The Committee observe that, so far these figures go, they tend to indicate a certain amount of shifting of the burden from the richer classes to the general population. The 25 per cent duty on sugar seems to be chiefly responsible for this, as it has the effect of raising the price of country as well as imported sugar

* See Report, para 145.

and thus to increase the burden of taxation on the poorest classes who are large consumers of both kinds.

§ 10. Abolition of the Cotton Excise Duty:—Throughout all the successive increases on imported cotton goods, the excise duty, as will have been noticed, remained at the same old level of $3\frac{1}{2}$ per cent. This paved the way for a complete abolition of this hated impost. In March 1925 the Legislative Assembly passed a Resolution in favour of the abolition of the duty and refused the grant for the excise staff. The depressing situation of the Bombay Cotton Industry led to a decision on the part of the millowners to reduce the wages of the mill hands by about $11\frac{1}{2}$ per cent. A labour deputation waited on the Viceroy in August 1927 and protested against the cut asking at the same time for an abolition of the cotton excise. This was followed by a millowners' deputation which urged the same measure. On 16th September, 1925, Sir Furshotamdas' Resolution was passed in the Assembly praying for the suspension of the duty. In November, Government issued an ordinance suspending the duty, which was finally abolished on 1st April 1926.

PROVINCIAL HEADS OF REVENUE

§ 11. Excise :—The excise revenue in British India is derived from the manufacture and sale of intoxicating liquors, hemp drugs, opium and so on. It is levied in the form of a duty on manufacture and fees for sale licenses. The major portion of the revenue is derived from country liquors. The system followed in regard to country liquor excise is that of granting by contract the right of wholesale supply for a district and selling by auction the right of retail sale. Two large distilleries in Bombay have been recently placed entirely under Government management thus partly suppressing the contract distillery system. In 1861-62 the excise revenue was Rs. 1,78,61,570 and expenditure Rs. 13,53,470. In 1924-25 the revenue was Rs. 19,51,68,438 and the expenditure 1,30,86,613. Whether this astounding increase of net revenue is to be looked upon as an index of growing drunkenness is a matter of controversy. Government explain it as being mainly the result of higher rates of excise duties, and

a stricter control, though it is also suggested that some of the increase is due to the expansion of population and the greater prosperity of certain classes.

Public opinion in this country is, however, seriously alarmed at what it regards as an unmistakable sign of increase of drunkenness. The Legislatures in the various provinces are bestirring themselves to grapple with the evil before it becomes even more serious than at present. The Bombay Council, for example, passed a Resolution in July 1924 in favour of total prohibition of liquor in 20 years.

Although there is a general agreement that energetic and courageous action is necessary for suppressing the evil of drink, there is no such agreement as regards the means to be adopted for this purpose. Government have so far relied largely on the method of raising the price of liquor as high as possible but not so high as to stimulate illicit production. Other steps taken to reduce the consumption of country spirit are rationing, reduction in the number of shops, lowering of the limits of possession, reducing the strength of the drinks supplied, curtailing the hours of sale, etc. Non-official opinion is inclined towards the restriction of quantity and a strict regulation of the number of shops together with a policy of local option and consultation of local opinion, in preference to high rates of excise duties. The Bombay Government has already adopted the policy of issuing fixed quantities annually on a progressively diminishing scale, so far as country liquor is concerned.

It has to be borne in mind that any impatient and drastic measures will be attended with the double difficulty of immediate and heavy loss of revenue and excessive expenditure for preventive establishment to put down smuggling and illicit distillation. These difficulties will clearly be most stupendous if complete prohibition at one stroke were to be attempted. Another danger to be guarded against is that, vice suppressed violently in one direction is apt to break out in another direction and often in a very much worse form. Thus it is complained that attempts to reduce the consumption of country spirit have in some cases been attended with an increased consumption of foreign

liquor and that people have even taken to methylated spirit in place of country liquor. The suppression of the evil in order to be completely successful must come as the result of a general realisation on the part of the people that drunkenness is a crime, and this is a matter of education. It should be remembered at the same time, however, that a wisely directed excise policy, besides decreasing the opportunities for indulgence, will also exercise a certain educative influence. The argument that reform must come from within and not from without must not be pressed to the point of denying any utility to measures whose intention is to increase the difficulties of excessive indulgence in drink. Such measures are useful at least in the case of those who are not yet definitely addicted to the habit and who will be saved if they are kept out of temptation's way.

The practical statesmen will bear in mind all these dangers and difficulties that are likely to obstruct the path of reform, and his policy will aim at achieving a happy commingling of daring and circumspection. He must honestly endeavour in this matter to relegate purely revenue consideration to an absolutely subordinate position and in so far as this is done we must expect a steady reduction in the revenue from excise hereafter.

§ 12. Other Sources of Revenue:—(i) *Stamps*:—Stamp revenue is derived from judicial and commercial stamps. The former represents fees on plaints and other documents in Civil and Criminal Courts. The latter represents duties on commercial transactions recorded in writing, such as conveyances as to the transfer of property, lands, bills of exchange and so forth. The revenue from judicial stamps is held by some to be not taxation proper, being a payment for the services rendered by a costly Department, viz., the Judicial Department.

(ii) *Forests*:—Indian Forests are a great Government asset and an important commercial Department systematically organised since 1864.* The revenue is derived mainly from the sale of timber and other produce, grazing fees and license fees for per-

* See Vol I, pp. 22-26.

mission to cut wood and other produce. The revenue is variable according to market conditions. Its future prospects are bright if the forests are properly nursed and exploited. The Provincial governments, to whom forests have been assigned, have been making a large net profit of about 150 lakhs per year in recent years. The net annual revenue was only about Rs. 14 lakhs between 1864 and 1870. Large initial expenditure, however, is necessary for ensuring a still more substantial and steadily growing revenue from forests.

(iii) *Registration etc.*:--The revenue from Registration is akin to judicial stamps revenue and is mainly derived from registration fees according to the value of the documents registered. Registration is compulsory in the case of certain documents relating to gifts and transactions in immovable property and optional in the case of others. Registration fees may be looked upon as payments for service rendered, the advantage lying in the consistency of deliberation, the publicity enforced on the parties and the provision of a record by way of satisfactory proof which may either prevent litigation or simplify its disposal by courts.

An entertainment tax on a graduated scale has recently been levied on amusements like cinema shows, dramas, etc. in Bombay, Poona, Karachi and Ahmadabad. In 1925, a Totalisator Tax on race course betting was levied in Bombay.

§ 13. Public Expenditure in India:--The following classification of public expenditure in India may be adopted.* (I) *National Defence*: Expenditure on army, navy, air force, frontier or strategic railways, harbours and defence works; military operations such as frontier expeditions etc.

II. *Maintenance of internal peace and order*:--(a) Expenditure on Police, Courts of Justice, Jails; (b) general administration; (c) expenses with regard to collection of revenue; (d) political charges including the expenses of the legislative machinery; foreign representation by consuls, ambassadors etc. (e) pensions, furlough allowances etc.

* K. T. Shah: *Sixty Years of Indian Finance* : pp. 44-46.

III. *National Development* :—Expenditure for (a) moral and (b) for material development. Under the former, may be included expenditure on education including scientific and miscellaneous departments, medical and sanitation charges; under the latter may be included expenses on railways, irrigation and public works, agriculture and famine charges, posts and telegraphs, interest on public debt [the interest on unproductive or dead-weight debt should strictly be included under (I) or (II)]

Table I below gives the principal heads of expenditure (central and provincial) and the proportion of public funds which each absorbs.

Table II shows the growth of public expenditure in India from 1858-59 to 1925-26.

Table I—Percentage expenditure (Central and Provincial)

No.	Name	1921-22	1923-24	1925-26
		per cent	per cent	per cent
1	Military Services	36	30	28
2	Railways	11	12	13
3	Public Debt	8	9	10
4	Police, Jails and Justice	9	10	10
5	Education	4	5	5
6	Civil Works	5	5	5
7	General administration	5	5	6
8	Land Revenue	3	3	2
9	Agriculture	1	—	—
10	Forests	2	2	1
11	Irrigation	2	2	3
12	Public Health	—	2	1

§ 14 Criticism of Public Expenditure in India:—The figures given in Table II below show a striking growth in public expenditure in India since the beginning of the present century, and more especially since 1913-14. As the late Mr. Gokhale pointed out long ago, an increase in public expenditure need not necessarily be a matter for regret and alarm. "Everything depends in this matter on the nature of the purposes for which the

† Table II—Growth of Public Expenditure in India (Central and Provincial).

(In crores of Rupees).

Year	Amount	Year	Amount
1858-59	50.19	1913-14	124.34
1870-71	49.39	1916-17	147.07
1880-81	52.64	1918-19	190.61
1890-91	51.98	1920-21	218.67
1898-99	58.29	1921-22	222.02
1899-1900	88.07	1923-24	206.48
1902-1903	78.34	1924-25	210.25
1910-11	115.12	1925-26	215.75

increase has been incurred and the results produced by such outlay of public money. In the United Kingdom, in France, in Italy—in fact—almost everywhere in Europe, there have been large increases in national expenditure....., but the increase in Indian expenditure.....differs from the increase elsewhere in a most fundamental respect. While increased expenditure in other countries, under popular control, ...has helped to bring increased strength and security to the nations, and increased enlightenment and prosperity to the people, our continually increasing expenditure has, under autocratic management, defective constitutional control and inherent defects of alien domination, only helped to bring about constantly increasing exploitation of our resources, has retarded our national progress, weakened our natural defences and burdened us with undefined and indefinite financial liabilities. Compelled to meet the demands of a forward Imperial frontier policy and the exigencies of conquest, Imperial defence and constant borrowing for commercial enterprises, often undertaken in consequence of the pressure of English commercial classes, our Indian Government has little money to spare, with

† The figures are given in rupees being converted at £ 1 : Rs. 10 'up to 1898-99 and at the official rate of £ 1 : Rs. 15 thereafter. Shah : *Sixty Years of Indian Finance*, p. 46.

all its increase of taxation, for purposes of national education..."^{*} Mr. Gokhale attributed a large part of the increase in public expenditure to the distrust and suspicion created by the Mutiny which led to the wider employment of the costly foreign services both in the civil and military branches. The most serious growth in public expenditure was caused during the War and post-War period. Our expenditure on military services was already high enough, viz., 29.84 crores of rupees in 1913-14, but it rose by leaps and bounds to Rs. 43.56 crores in 1917-18, 66.72 crores in 1918-19 and 67.38 crores in 1920-21. Since then it has been reduced to 54.92 crores in 1927-28 (Revised Estimates), and has been placed at Rs. 55.10 crores in the budget estimates for 1928-29. The Inchcape Committee (1922-23) recommended an immediate reduction of the military expenditure from Rs. 67.38 to Rs. 57.75 crores and urged that the Government of India should not remain satisfied with this but should keep a close watch on the details of military expenditure so as to bring it down after a few years to a sum not exceeding Rs. 50 crores. This figure, however, has not yet been quite attained. The methods of economy that have been suggested from time to time are reduction of the size of the army to the minimum required for strictly Indian purposes, continuous and progressive Indianisation so as to avoid the expensive recruitment in England through the British War Office and the heavy non-effective charges. The introduction of a short military service under the voluntary system has also been suggested instead of maintaining the army during times of peace practically on a war establishment.

Putting together provincial and central expenditure the army accounts for 28 per cent of the total expenditure (the percentage would be much higher if only the central expenditure were to be taken into account). The argument from percentages is not in itself conclusive as regards the question whether the military expenditure is heavier than it ought to be. Safety being a matter of paramount concern from the economic and every other point of view, almost every sacrifice must be undergone in order to secure it. The amount which a country must spend on defence will

^{*} Written evidence of the late Mr. G. K. Gokhale before the Welby Commission, 1897.

depend upon the character and intentions of possible enemies, the extent of vulnerability of the country's natural frontiers etc. To show therefore that the burden is crushing or that it is higher in comparison with what some other countries have to bear is not necessarily to condemn the actual scale of expenditure. All this is perfectly true. We must, however, beware of making a fetish of military efficiency. We must also remember that a very poor country like India must, within certain limits, be prepared to take risks for the sufficient reason that she cannot afford to aim at an absolutely perfect state of readiness to meet all conceivable contingencies. Complete national safety may be secured on these lines but the burden on the people will be so heavy as to make life for them not worth living.*

Popular Indian opinion holds that all practicable economies even though fully compatible with safety, have not been carried out consistently and that military expenditure has been allowed to swell to unreasonable limits with the consequence that the nation-building activities have been starved.† In spite of Government's protestations to the contrary, the belief is widely held that there is still considerable room for economy in military expenditure. It is remembered that Government have always protested that the utmost economy is being practised. And yet the Inchcape Com-

* " We do not object to the fire being kept up, but to the absence of any cooking pot over it. And when the cost of the blaze becomes so exorbitant as to leave nothing over to fill the pot with, then, if in answer to the tears which spring from the gnawing emptiness within, the question is thundered against us, " Are we not then to light up your hearth ?" we have to falter back, " Yes, yes no doubt, but not for our cremation please!" Rabindranath Tagore in Modern Review, June 1925.

† " The following figures from the Indian Year Book and Statesman's Year Book are well worth noting :—

	1913-14	1927-28	Increase per cent
India (Rs. crores) ...	31.5.	56.7	80
Britain (£. m.) ...	74.5	115.1	55

The rise of prices has been about the same in both countries. It is obviously absurd to maintain that India's responsibilities in the matter of defence are now greater than those of Britain herself. " Prof. R. M. Joshi's Paper before the Economic Conference, Mysore, 1929.

mittee, in spite of the fact that its terms of reference did not allow it to consider certain fundamental aspects of army retrenchment, was able to recommend a substantial reduction and government did not find it impossible to carry out the economies suggested almost completely. People naturally though perhaps illogically argue that the economies already effected prove that still more economies are practicable. So long as the military administration remains outside the control of the chosen representatives of the people and so long as no Indians are admitted within the inner councils of the Army, so long this attitude is bound to persist and military expenditure will continue to figure as one of the major popular grievances against the Government.

The enormous increase in the expenditure on civil administration has been another never-ending subject of criticism, the general complaint being that the Indian administration is one of the costliest in the world and that the scale of salaries and allowances given to the higher services, until recently manned almost exclusively by Europeans, is excessive. The Reforms have further added to the costliness of the administration in a variety of ways. The increases in salaries, allowances and other concessions recently granted by the Lee Commission and estimated to add to the national expenditure to the extent of Rs. 1½ crores annually, have been criticised as wholly unjustifiable on the ground that the original scales of pay were so high that no revision was called for in spite of the recent rise in prices. The real remedy is one that has been repeatedly suggested, viz. rapid Indiansiation with a reduction in the scale of the salaries. The economies effected in this manner will not be attended with any fall in efficiency provided the principle of communal preferences is either abandoned or applied as sparingly as circumstances permit. If preferences have to be given to certain communities in public employment, certain minimum educational and other qualifications should be insisted upon, and as far as possible, selections even within a given community should be governed by competitive tests.

It is thus of the greatest importance that there should be a rigorous pursuit of economy in all the branches of administra-

tion and those in charge of public funds should realise, in a fuller measure than is usual, the fiduciary position which they occupy with regard to the taxpayer and display a more exact diligence in the manner in which these funds are administered. We must however add that it is equally necessary that the folly of unlimited parsimony should be recognised and expenditure should be as liberal as possible on departments like education, agriculture, industries, irrigation, etc. For unless money is freely spent on them the economic uplift of the people cannot be achieved.

§ 15 Burden of taxation.—The Statistical Abstract of British India (1925-26) gives the following figures bearing on the burden of taxation in India.

In crores of rupees.

	1921-22	1925-26
Total Taxation (including land revenue)*	1,25,13	1,40,12
Payment per head based on Census population in 1921	Rs. as. p. 5 1 1	Rs. as. p. 5 10 9

Sir Purshotamdas Thakurdas in his speech as a member of the Commercial Deputation on retrenchment to His Excellency the Viceroy gave the following estimates of the incidence of taxation. ‡

1871	Rs. 1-13-9	1911	Rs. 2-11-3
1881	„ 2- 2-3	1913	„ 2-14-5
1901	„ 2- 6-6	1922	„ 6- 1-8

According to these figures the nominal incidence of taxation in 1922 was more than double what it was in the pre-war period. But whether this represents a real higher burden depends on the

* We have already referred to the view of the Taxation Enquiry Committee that land revenue ought to be regarded as part of the burden of taxation. See vol I. p 445.

‡ Quoted by Vakil : *Financial Developments*, Table 42, p, 460.

figures we adopt for the per capita incomes for the two periods.*

It is sometimes argued that because the per capita incidence of taxation in India bears a lower ratio (something like $\frac{1}{12}$ th) to the income per head, therefore the Indian burden of taxation is light as compared to countries like Great Britain where the proportion of national income absorbed by taxation amounts to more than 23 per cent. This is however a superficial view because the lower proportion of a low national income may represent a very much heavier burden than a higher percentage of a high income. Another obvious point is that the relative pressure of taxation in different countries cannot be considered apart from the nature of the services rendered by the state to the people in return for the taxes it levies.

§ 16. Distribution of the Burden of Taxation:—The problem of the incidence of taxation is one of the most complicated subjects in economic science and is rendered more so in India owing to lack of precise statistical information regarding the income per capita and the distribution of the national income. Under these circumstances the Taxation Enquiry Committee are thrown back on such general considerations about incomes and standards of living of typical classes of the population as a prudent Finance Minister would examine in framing or revising a scheme of taxation. They select a few typical classes of the population and offer certain tentative conclusions regarding their position as it exists at present and as it would be in the event of certain changes in the taxation system being introduced. The Committee find that the burden on none of the classes is oppressive though its distribution is unequal. Some of them escape their proper share of taxation e. g. the bigger landlords, and the village trader who might well be brought within the scope of further taxation by a more general and a more efficient administration of the circumstances, property and profession taxes.† Before the War, taxation was very unevenly distributed between the

* See p. 186, above.

† See Taxation Enquiry Committee's Report paras 478-492

different classes of the community. The poorer sections of the community bore the brunt of the burden in connection with the land revenue, salt tax, excise duties, stamps, etc; while the richer sections were able to resist their just share of taxation. The War and the post-war changes in taxation, while they have certainly increased the burden on the masses, have partially removed this blot on the taxation system of the country and made the incidence somewhat more equitable by the introduction of a graduated income tax, the super-tax, the levy of special import duties on luxury articles etc.

The Taxation Enquiry Committee make various proposals * to redress the inequalities till further. For instance, they hold that, while the Indian rates of Income Tax are comparable with those in other countries they are decidedly low in the case of incomes from £ 1,000 to £ 10,000, for which therefore they propose higher rates of taxation. They also recommend the reduction of the exemption limit for the super-tax to Rs. 30,000, a new rate of super-tax, and a reduction of the exemption limit in the case of a joint Hindu family to Rs 60,000. They favour the removal of the duties on kerosene and sugar as pressing disproportionately on the poorer sections of the community. As likely to be borne mostly by the richer classes they suggest an excise duty on aerated waters, on cigarettes and pipe tobacco, licensing for country tobacco, increase in the license fees for firearms, etc.

§ 17. Taxable capacity:—In the words of Sir Josiah Stamp,† “Taxable capacity or fund is measured by the difference between the two quantities—the total quantity of production and the total quantity of consumption.” In the case of India the standard of consumption is very low, but, as we have seen, production also is very low, so that the difference between the two gives us a very small margin of taxable capacity. It is however impossible to say with any degree of precision what this margin is exactly. In discussing the national income of India we have

* The Committee was appointed in 1924 to examine the manner in which the burden of taxation was distributed and to consider *inter alia* whether the whole scheme of taxation, central, provincial and local was scientific and equitable.

† *Wealth and Taxable capacity*, p. 114.

already commented on the paucity and unreliability of the available statistical data which makes it possible for people to pick and choose their evidence and present a bright or gloomy picture, as may suit them, of the economic condition of the masses. For obvious reasons the same remarks apply to calculations of taxable capacity. However we give the following calculation* rather as illustrating the method of computation (which, we believe, is all it is intended to do) than as a thoroughly dependable estimate of taxable capacity on which actual practical policy might be based.

Taxable Capacity of British India. (Figures in lakhs of Rs.)

Details	1910-11 (Census 1911)	1920-21 (Census 1921, a distinctly bad year).	1921-22 (Good for ag- riculture, but year of Trade Depression).
1. Income :			
Agricultural ...	1412,00	1715,00	1983,00
Non-agricultural ...	530,00	883,00	883,00
Total income ...	1942,00	2598,00	2866,00
2. Allow for minimum consumption ...	1214,00	2220,00	2220,00
3. Allow for seed and manure ...	141,00	172,00	198,00
4. Allow for replacement of & ordinary additions to capital ...	25,00	45,00	55,00
5. Taxable capacity(1,2,3,4)	562,00	161,00	393,00
6. Tax revenue:			
Central and Provincial Governments ...	79,83	130,15	135,30
Local bodies ...	7,17	11,64	11,64
Total ...	87,00	141,79	146,94
7. Expenditure on inter- nal debt:			
Central and Provincial Governments ...	5,61	21,04	24,27
Local bodies ...	1,70	2,34	2,34
Total ...	7,31	23,38	26,61
8. Effective taxation(6-7)...	79,69	118,61	129,33
9. Balance (5-8) ...	482,31	42,39	272,64

* Taken from Findlay Shirras : *The Science of Public Finance*, p. 146,

The figures for taxable capacity and the balance of it still remaining untaxed which emerge from the above calculation must not lead the reader to suppose that it gives the practical limit to which taxation could be increased if necessary. Government themselves have admitted several times that the limit of taxation has for the present been reached. Small increases here and there may be possible but the principal hope lies in reduction of expenditure and the application of public funds in such a manner as eventually to increase the wealth and taxable capacity of the people.

Small beginnings, however, might be made by way of striking out new paths of revenue expansion. The Taxation Enquiry Committee, for example, show a decided bias in favour of an income tax on the higher agricultural incomes. They point out that the inequality between the landholders of different classes is aggravated by the absence of an income tax on agricultural incomes or a death duty, which serves in the more advanced countries to introduce an element of progression in the tax on land. Duties on inheritance and succession are a source of considerable revenue in countries like England and are recognised as a desirable form of taxation, since they fall pre-eminently on accumulated wealth. The medley of customs in respect of inheritance, the joint family system and other factors would make the introduction of inheritance taxes in India difficult. But so far as may be practicable, we think that a beginning should be made in the taxation of agricultural incomes as well as in the direction of inheritance and succession duties. It is necessary that the country should be willing, after due consideration, to try fresh experiments in taxation which have been found successful elsewhere. We do not suggest that any considerable increase in Government revenue by additional taxation in any form is immediately practicable, but we plead for a constant readiness to explore fresh possibilities of taxation. In taxation, as in other matters, the prevalent tendency in India of opposing new ideas merely because they are new is to be deprecated. If mere fashion or novelty is the law of one set of fools, it must be remembered that custom or precedent is the sole legislator of another set of fools. A con-

siderable amount of money may indeed be saved by stopping all wasteful expenditure and this policy should be pursued with the utmost vigour. Money thus saved however will not be enough for financing the many-sided development of which the nation is thinking and additional taxation will be necessary if progress is to be rapid and substantial.

§ 18. Recent Indian Finance:—Owing to limitations of space it is impossible for us to enter into anything like a detailed history of Indian finance under the East India Company and the Crown. The confusion between the commercial and administrative accounts under the East India Company, the chronic deficits which characterised the administration of the Company, the financial burdens of the Mutiny, the appointment in course of time of a regular Finance Member, the gradual progress in financial decentralisation, the embarrassments caused by famines, frontier wars and fall in exchange, the loan policy of government, the budget surpluses of the pre-War years roughly since the beginning of the present century—these are some of the topics belonging to the history of Indian Finance. We shall have something to say on one or two of these topics in greater detail, but for the present we propose to take note of the principal happenings in the domain of Indian finance since the outbreak of the War.

The smooth course of India's pre-War finance and the era of budget surpluses came to an end abruptly with the outbreak of the War in July 1914. The dislocating effect of the War on trade and industry was immediately reflected in the conversion of the surplus of Rs. 1.8 crores to a deficit of Rs. 2.6 crores in 1914-15. The budget for 1915-16 also showed a deficit of 1.7 crores. As the War was expected to last only for a short period the Government decided to meet the deficit by temporary borrowing and by drawing on the balances in England so as not to disturb the existing level of taxation. The programme of capital expenditure on Railways and Irrigation were also considerably reduced. The expectation, however, that the War would be a short-lived one was doomed to disappointment. Important changes in taxation in the budgets of 1916-17 and 1917-18 became inevita-

ble and rigid economies my was ordered in all the departments except the army department. The budget for 1916-17 provided for an increase in customs duties, income-tax, salt duty and excise duties. We have already dealt with the details of War taxation of this and the following years. In the budget for the year 1917-18 further increases in taxation became necessary in order to meet the cost of the War contribution of £. 100 millions to his Majesty's Government. The contribution was to be provided for by raising War Loans in India, as the English money market was fully occupied with the British War demands, and by taking over a part of the British War debt to the extent that the Indian loans fell short of the promised amount. The War contribution involved an annual burden of Rs. 9 crores for interest and sinking fund charges, and to meet this, increased taxation was resorted to in the form of the super-tax, rise in the cotton import duty to $7\frac{1}{2}$ per cent, doubling the export duty on jute and levying a surcharge of Railway goods traffic. The increase of taxation and excessive caution in framing the budget together with retrenchment resulted in a large surplus in the year 1916-17 (11.2 crores) and 1917-18 (12.12 crores). There was no necessity, therefore, to resort to further taxation in 1918-19, though the existing level of taxation was maintained. In 1918-19, however, owing to the promise by the Government of India of a further War contribution of £. 45 millions (a figure which was ultimately reduced), additional taxation became necessary and the excess profits tax was levied for one year. During the period 1914-15 to 1918-19 the central revenues showed a substantial increase from Rs. 76.1 crores to Rs. 130.04 crores and central expenditure from 78.8 crores to 136.1 crores.

The most acute problem of war finance was created by the large disbursements which the Government of India had to make on behalf of the British War Office aggregating to £. 240 millions during 1914-19. The Secretary of State, as we have seen, had to sell Council Bills beyond his requirements for financing the essential exports and the joint strain of the large War disbursements and the encashment of the Council Bills created a difficult situation with regard to the ways and means programme. The principal resources were the proceeds of War loans in India, the

Central and Provincial surpluses which had accrued, the issue of Treasury Bills, the expansion of paper currency against the holdings of the British Treasury Bills in London and later on against the 'created securities', and lastly the heavy coinage of silver obtained from U. S. A. under the Pittman Act.*

§ 19. Deficit Budgets:—In contrast with the budget surpluses which especially characterized the pre-War period, there now set in a succession of deficit budgets both in Central and Provincial finance. In five years the aggregate deficit in the budgets of the Central Government alone amounted to nearly 100 crores of rupees. On the top of the additional expenditure due to the European War, there was also the trouble caused by the wanton invasion of India by Afghanistan which cost the Indian exchequer several crores of rupees. Again, the cost of civil and especially of military administration went on increasing year after year. The expenses of Railway operations also showed a heavy increase and the Railway receipts suffered owing to post-War trade depression which followed on the heels of a short-lived boom. Apart from diminished railway receipts there was also the decreased yield from the income-tax. The cumulative effect of all these factors was seen in the continuance of heavy deficits inspite of large increases in taxation between 1914-1922.

In 1922-23 the Retrenchment Committee was appointed to suggest means of reducing the overgrown expenditure of the Central Government. The Committee suggested several cuts aggregating to Rs. 19½ crores as follows:—Military expenditure Rs. 10.5 crores; Railways, Rs. 4.5 crores; Civil Administration, Rs. 2.19 crores; and Posts and Telegraphs, Rs. 1.3 crores.† In 1923-24, a reduction of 6.6 crores in the non-military expenditure and 5.75 crores in the military expenditure was effected. But this did not suffice to restore budget equilibrium and, as we have seen, the Viceroy felt compelled to double the salt tax from Rs. 1-4 to Rs. 2-8. Since 1923-24 the tide has turned and there has been a reversion to the old tendency of surplus budgets due to excessive caution in revenue estimates, the stabilisation of the Rupee at 1s. 6d., the retention of the high level of taxation

* Panandikar: *Economic Consequences of the War for India*.

† See Report of the Retrenchment Committee, pp. 429-30.

previously introduced and the gradual recovery of trade and industry. These surpluses have been utilised for abolishing provincial contributions and reducing the unproductive debt.

§ 20. Central and Railway Budgets:—We shall conclude this section with a general statement of revenue and expenditure charged to revenue of the Central Government. Considerations of space do not permit of a detailed discussion of the revenue and expenditure of the railway administration. All we can do is to mark our sense of its importance by finding space for the most recent railway budget. (See pp. 585-586).

§ 21. The public debt in India:—The origin of our public debt is to be traced to the wars of the East India Company which had steadily taken up the figure for national debt from £ 7 millions in 1792 to £ 59½ millions just before the Mutiny in 1857-58. In the following year the figure rose to £ 60½ millions. The whole charge of the Mutiny was thrown on India so that the total public debt amounted in 1860 to over £ 100 millions. When the Company's rule was abolished in 1858, the Government of India not only assumed responsibility for the territorial and other debts of the Company but also for the payment of the dividend on the capital stock of £ 12 millions of the East India Company, until in 1874 the East India stock was redeemed. The debt inherited by the Government of India from the Company was purely unproductive. Since 1867, however, when the policy of constructing "extraordinary public works" (or 'productive works' as they came to be called later on) like railways and irrigation commenced, there has been a steady growth in the amount of productive or Public Works Debt as distinguished from "Ordinary Debt" as the unproductive debt came to be called from 1879. Additions to this debt were made when Government had to borrow for purchasing some of the railways from the Companies or for making advances to them. In conformity with the recommendations made by the Select Committee of 1878 the surplus revenue of a particular year was not applied to the cancellation of debt but on productive works for which Government would otherwise have been required to borrow. The reduction of the 'ordinary' debt was thus automatically followed by a

Central Budget. (In lakhs of rupees.)

	1921-22 Actuals	1928-29 Budget Estimates		1921-25 Actuals	1928-29 Budget Estimates
Revenue:—			Expenditure—		
Principal heads of revenue :			Direct demands on		
Customs	34,40	50,18	the Revenues	5,27	4,24
Taxes on income	18,74	16,99	Salt and other ca-		
Salt	6,34	7,00	pital outlay cha-		
Opium	3,07	3,47	rged to Revenue	...	6
Other Heads	2,20	2,20	Railways: Inter-		
Total principal			est, miscellane-		
Heads	64,76	79,85	ous charges as		
Railways: net			per Railway Bud-		
receipts as per			get	24,29	33,02
Railway Budget	15,20*	38,50	Irrigation	14	23
Irrigation; net			Posts&Telegraphs	1,66	81
receipts	5	12	Debt services	15,99	14,90
Posts&Telegraphs			Civil administra-		
Net Receipts	56	57	tion	9,40	11,69
Interest Receipts	1,11	2,91	Currency, Mint		
Civil administra-			and Exchange.	1,07	69
tion	77	1,01	Civil Works	1,54	1,73
Currency & Mint	437	2,48	Miscellaneous	5,58	4,10
Civil works	11	14	Military Services	77,87	58,04
Miscellaneous	7,18	81	Miscellaneous ad-		
Military Receipts	8,06	2,94	justments bet-		
Provincial contri-			ween Central		
butions and mis-			and Provincial		
cellaneous adjust-			Governments.	...	...
-ments between			Extraordinary		
Central and Pro-			items	...	4
vincial Govts.	12,98	...	Total expenditure	1,42,86	1,29,59
Extraordinary			Surplus	...	5
items	...	26			
Total Revenue	1,15,21	1,29,64	Total ...	1,42,86	1,29,64
Deficit	27,65	...			
Total ...	1,42,86	1,29,64			

*There was no separate railway budget till 1925-26.

Railway Budget for 1928-29- (In crores of rupees).

<i>Heads of Revenue.</i> State Railways.		<i>Heads of expenditure.</i> State Railways.	
(a) Commercial lines.—		Interest : Commercial lines:—	
Gross Receipts	101.65	On Government Capital at charge.	26.07
Deduct-working expenses	62.61	On capital contributed by Indian States and Companies.	1.52
Surplus profits paid to Indian States and Railway Companies	1.82		
Net Receipts	37.21	Total interest, Commercial lines.	27.59
(b) Strategic lines.—		Interest, strategic lines.	1.40
Gross Receipts	1.59		28.99
Deduct-working expenses	1.87	Subsidised companies:	
Net Receipts.	-.28	Land and Subsidy.	.10
Total net receipts, Commercial and strategic lines.	36.94	Miscellaneous Railway Expenditure.	.42
Subsidised companies : Govt. share of surplus profits.	.46	Payments to General Revenues:—	
Miscellaneous Railway Receipts:		Contribution*	5.22
Interest, Depreciation and Reserve Fund Balances.	1.04	One-third of the excess Railway surplus over three crores.	.25
Dividend on investments in branch lines and other miscellaneous Receipts.	.05	Total payment to General Revenues.	5.48
		Surplus Railway Revenue Transferred to Reserve.	3.50
Total Receipts.	38.50	Total Expenditure.	38.50

* This amount is arrived at as follows (Based on Actuals of 1926-27):—

(1) 1 per cent on capital of Rs. 6,29,56,41,923 = Rs. 6,29,56,519

(2) $\frac{1}{5}$ th of surplus Rs. 2,83,51,938

(Receipts Rs. 98,57,50,966—charges such as working expenses, interest, etc.

Rs. 95,73,99,028 on commercial lines.) Rs. 56,70,388

Total contribution from Railways to Revenues Rs. 6,86,26,907

(3) Deduct—Loss on strategic lines borne by Railway Revenues (Interest on capital of Rs. 31,60,50,135 = Rs. 1,31,35,059 + loss in working Rs. 32,07,200).

Rs. 1,63,42,259

Net payment due from Railway to General Revenues in 1928-29. Rs. 5,22,84,648

(continued from page 584)

an equivalent increase in the public works debt" By this process the ordinary debt would have been wiped off altogether by 1917 but for the huge addition to the debt for which the War was responsible. The late Mr. Gokhale was a strong critic of the policy of utilising the surplus revenue for reducing the ordinary debt and increasing the productive debt. He contended that in view of the smallness of the unproductive debt, there was no need to liquidate it out of Government's ordinary surpluses which ought to have been returned to the taxpayer by remission of taxation or, better still, spent on beneficial non-recurring expenditure such as education, medical relief, etc.. to be met from special provincial reserves to which the Imperial Government might have made grants from their surpluses.

By far the greater portion of the public debt of India during the pre-war period was raised in England. Government defended this policy on the ground that the difference between the rates of interest in India and in England was so considerable as to counterbalance any disadvantages attendant upon borrowing in England. They had also a very poor idea of the resources of the Indian money market, whose maximum lending capacity in any single year they put at not more than Rs. 5 crores. It was left to the War and the post-war period to prove that this was very much of an underestimate. During this period the ordinary debt increased rapidly from Rs. 3.1 crores on 31st March 1916 to Rs. 257.70 crores on 31st March 1924. This was due to India's war contribution of £100 millions,* the expense on new Delhi and the post-war era of successive deficits in the budget of the Central Government for 5 years. Successive war loans were raised in India to meet these demands, as the English money market was fully taxed by the demands made on it by the English Government for war purposes, and Government were able to get the unprecedented amount of Rs. 53 crores in 1917, and Rs. 57 crores in 1918. The strength of the Indian money market

* An additional war contribution of £ 45 millions was promised in 1918 in the event of the war being prolonged. But in 1919-20 in view of the heavy expenditure of £ 16 millions due to the Afghan war, the additional war contribution was substantially reduced.

for Government loans, first revealed during the war period, has been largely maintained during the post-war years, and Government now do most of their borrowing for productive purposes in the country itself. Apart from the large amounts raised by the War loans another welcome feature of these loans was the increase in the number of investors, thanks to effective advertisement and offer of increased facilities in regard to the administration of the Public Debt at Government treasuries and sub-treasuries. In this connection special mention must be made of the Post Office branch of the war loans and the cash certificates which have since become a permanent feature of Government's loan policy.

Another innovation which owed its birth to the War was the introduction of Treasury Bills first issued in 1917 for meeting Government's disbursements on behalf of the British War Office. They were again resorted to for financing the deficits in the post-war period, when the old bills were paid by issuing new bills. Ultimately the large outstanding amounts of Treasury Bills were reduced by discharging the Treasury Bills from the proceeds of long-term loans—a questionable procedure from the point of view of sound finance.

§ 22. Rupee and Sterling Loans:—The loans raised in India are called rupee loans or rupee debts, as they are subscribed in rupees and the interest and principal are paid in rupees. It must not, however, be supposed that the rupee loans are necessarily internal loans or even held wholly by Indians. The bulk of the Rupee Debt is held in India, but a certain portion is held by investors who live in England and receive their interest in that country. Again, the Rupee Debt held in India is divided between Indian and European investors. It has been suggested that all debt, whether rupee or sterling, whether held in India or England, should be considered as external if held by non-Indians, and internal if held by Indians.* Judged by this standard the major portion of our debt is external. It need scarcely be added

* Gyan Chand: *Financial System of India*, p. 312.

that the policy should be to reduce the volume of the external debt as far as possible, because it creates all kinds of political difficulties and also complicates the Indian exchange problem.

§ 23. Debt redemption:—In the pre-war period, the Public Debt of India was being reduced in two ways. One of these has been already noticed, viz., the utilisation of surpluses for capital expenditure on railways, irrigation, etc. which enabled the Government to avoid borrowing and to reduce the unproductive debt to that extent. The second method was adopted for meeting the liability incurred in connection with the purchase of certain railways. A portion of this liability was and is being reduced under the statutory obligation of payment of railway annuities (issued in repayment of both principal and interest on loans). So also the India stock for which the shareholders of railways were permitted to exchange their annuities and the securities of the original Companies, from which the railways were purchased, is being reduced from certain sinking funds shown under Railway account. During the war, a sinking fund was established in connection with the issue of the 5 p. c. War Loan of 1917. Government undertook to set aside $1\frac{1}{2}$ p. c. of the amount of the loan for the purchase and cancellation of the loan securities, so long as their market price was below the issue price. In addition to this, Government have been making annual provision to the extent of nearly £500,000 for meeting India's liability in respect of the unpaid portion of the war contribution. Government have also made provision for the optional payment of an extra 80 lakhs voted since 1921-22 for an additional depreciation fund for the 5 % loan.

But the position so reached was largely the result of accident and the whole question of the redemption of public debt had never been reviewed in a scientific and systematic manner. A well-devised scheme for debt redemption is however essential in order to maintain both the external and internal credit of the country unimpaired, so as to facilitate renewals of maturing debt and the raising of such new capital as may be required at reasonable rates of interest. Recently a regular debt redemption scheme was accepted by the Assembly in December 1924 on the initiative of Sir Basil

Blackett. In enunciating the principle of the scheme Sir Basil Blackett suggested that the best way of arriving at a regular programme of debt redemption was to take the gross total of the debt, examine the capital assets held against it and fix the appropriate period within which it is desirable to amortise each category of debt. On this plan, the Finance Member announced a scheme on the 9th December 1924, under which, for a period of 5 years in the first instance, the annual provision for the reduction or avoidance of debt to be charged against annual revenues was fixed at Rs. 4 crores a year plus $\frac{1}{80}$ th of the excess of the debt outstanding at the end of each year over that outstanding on 31st March 1923. * As Sir Basil Blackett made it clear, the provision for the sinking fund so proposed would operate not to reduce the net total debt as long as there is a considerable annual programme of new capital expenditure, but to reduce the unproductive portion of it. The amount thus provided becomes a contribution out of revenue towards productive capital expenditure. The provision, therefore, is better described as a contribution out of revenues for the reduction or avoidance of debt than as a sinking fund.

Financial Relations between the Central and the Provincial Governments.

§ 24. Historical Summary:—From 1833 to 1871, all financial powers were in the hands of the Government of India which controlled the smallest details of Provincial expenditure. The whole of the revenues were paid to the account of the Government of India and the Provincial Governments only got fixed contributions to meet their expenses. This led to extravagance, rigidity and friction in Provincial finance and uncertainty in Central finance.† But gradually as a result of the system of periodical financial settlements first begun by Lord Mayo in 1871

* See *India's Parliament*, Vol. X, p. 275.

† "The distribution of the public income degenerated into something like a scramble, in which the most violent had the advantage with very little attention to reason. As local economy brought no local advantage, the stimulus to avoid waste was reduced to a minimum and as no local growth of the income led to local means of improvements, the interest in developing the public revenues was also brought down to the lowest level." Sir Richard Strachey.

and further improved in 1877 and 1882, the Provinces had come to enjoy a larger share of the revenues raised within their borders and greater freedom in regulating their expenditure. Certain heads of revenue and expenditure came to be shared between the Central and Provincial Governments in a rather complicated manner. The settlements were at first revised every five years, but as this led to a want of continuity of financial policy, they were made quasi-permanent in 1904, liable to revision only if there was a substantive change in the original conditions or if there was an emergency like war or famine.

The settlements were declared to be practically permanent in 1912 and the allocation decided upon was as follows:—On the revenue side the Central Government retained for its use all the revenues which could not be allocated or traced to any province, these being called the Imperial Heads of Revenue, such as Opium, Railways, Customs, Salt, Mint and Exchange, Posts and Telegraphs, Military receipts and tributes from Native States. Of the remainder some were wholly provincial like Forests, Excise (in Bombay and Bengal), Registration, and the departmental receipts from such provincial departments as Education, Law and Justice. Lastly, there was an important class of divided heads of revenue like Land Revenue, Income Tax, Excise (except in Bombay and Bengal), Irrigation and Stamps. Receipts from these were divided between Imperial and Provincial Governments in stated proportions, generally equal, but determined separately for each province. On the expenditure side a somewhat similar arrangement prevailed, and there was a special arrangement for the sharing of expenditure on famines. The pre-Reform system suffered from the following main defects:—(1) The divided heads of revenue in which both the parties were interested were a source of constant interference on the part of the Central Government and hampered provincial development. (2) The occasional 'doles' given by the Central Government to the Provinces out of its surpluses had a dislocating influence on Provincial finance. (3) Serious inter-provincial financial inequalities were created. (4) The Provincial Governments had no independent powers of taxation. (5) Too detailed a control was exercised over the provincial budget and expenditure by the Central Government.

The Provinces, for example, could not budget for a deficit nor could spend their balances freely.

§ 25. Financial Relations since the Reforms:—Since the Reforms the fiscal relations with the Central Government have been radically changed. As the new policy of Responsible Government was to be tried in the Provinces and as provincial financial autonomy or financial devolution was recognised to be the keynote of the Reforms, it was deemed necessary to abolish the divided heads of evenue, in order to give effect to the new principle, and the new allocation of revenue and expenditure was as follows:—(A) *Imperial Heads of Revenue*:—Opium, Salt. Customs, Income-tax, Railways, Posts and Telegraphs, Military receipts (B) *Provincial Heads of Revenue*:—Land Revenue, (including Irrigation); Stamps, judicial and commercial; Registration, Excise and Forests.

§ 26. The Meston Award:—The abolition of divided heads of revenue and the provincialisation of some heads like the Land Revenue and Stamps resulted in a Central or all-India deficit of Rs. 983 lakhs, which had to be provided for by a scheme of provincial contributions to the Central exchequer. A Committee was appointed under the chairmanship of Lord Meston to consider this and other allied questions. The Committee's decision with regard to the distribution of this burden (the Meston Award as it is called) is summarised in the following table:—

Initial Contributions and Standard Contributions.

*Province	For 1921-22 (in lakhs of Rs.)	Standard Contributions
Bombay ...	58	13-90 ths
Madras ...	348	17-90 ths
Bengal ...	63	19-90 ths
United Provinces ...	240	18-90 ths
Punjab ...	175	9-90 ths
Burma ...	64	6½-90 ths
Central Provinces and Berar ...	22	5-90 ths
Assam ...	15	2½-90 ths
Total ...	983	90

* It will be noticed that Bihar and Orissa escapes altogether.

The initial contributions were confessedly arbitrary and were based upon the increased spending power of the provinces due to the new distribution of the revenue heads, and the only consideration that was borne in mind was so to fix the contribution of each province that it should not be confronted with a deficit or compelled to resort to new taxation. Thus Madras was to pay 348 lakhs of rupees because the improvement in its spending power was Rs. 576 lakhs; Bombay, on the other hand, paid only 56 lakhs because the improvement in its spending power was 93 lakhs and so on. The standard contributions were based on the capacity to pay of each province as judged by such factors as population, income tax receipts, etc., and were to be worked up to by regular gradations in the seventh year beginning from 1921-22.

§ 27. Abolition of Provincial contributions:—The Meston Settlement did not please anybody and caused a good deal of provincial discontent. For, while the industrial provinces like Bombay and Bengal could never reconcile themselves to the virtual loss of the income-tax revenue, the agricultural provinces like Madras, the Punjab and U. P. resented what they considered their excessive initial contributions. The contributions were felt to be peculiarly burdensome when the Provincial Governments were faced with a series of deficits. The revenues assigned to them, such as Land Revenue, were inelastic and inadequate for meeting occasional contingencies or even the expenses of normal development. There was thus an unceasing clamour for the abolition of the contributions. The gradual improvement in the finances of the Central Government made the extension of some relief possible in 1925-26, when Rs. 250 lakhs, out of a total surplus of Rs. 324 lakhs, was utilised for granting permanent remissions of contributions to Madras (Rs. 126 lakhs), U. P. (56 lakhs), the Punjab (61 lakhs), and Burma (7 lakhs). In the next Budget statement a further sum of Rs. 125 lakhs was remitted in favour of the same provinces. In 1927-28, the entire amount of the outstanding contributions was remitted and finally relinquished in 1928-29,

Thus the provinces have at last shaken themselves free from the ugly nightmare of these oppressive levies

§ 28. Problem not yet solved:—It must not be supposed, however, that the final extinction of the provincial contributions has put an end to all controversy regarding the division of revenue between the Central and Provincial Governments. The main grievance of the Provinces, especially of the industrial Provinces like Bombay and Bengal, still remains, and this is that the Central Government has taken for itself growing sources of revenue like the income-tax and customs, and left for the provinces inelastic sources like land revenue and excise. The land revenue is fixed for long terms and moreover there is a great disinclination on the part of the people to submit to additional increases of it. The excise revenue must decline as steps are being taken to introduce prohibition in response to a strong popular demand. In fact the Provinces complain that the process of decline is not as fast as they would like to see it. They hate the very touch of the tainted excise revenue, but are compelled, on pain of bankruptcy, to clasp it in what threatens to be an eternal embrace. The forest revenue requires liberal capital outlay before it can be appreciably expanded. The stamps revenue cannot easily be increased further. On the other hand the provinces are responsible for nation-building departments, such as education, medical relief, agriculture etc. on which heavy outlay is essential. Famine expenditure has also been put on the shoulders of the Provincial Governments. The Bombay Legislative Council pointed out in their representation to the Government of India in March 1925 that the distribution of surplus revenue assigned to the provinces under the Reforms was determined in a haphazard manner and bore no relation to the needs of the provinces or to the total taxation derived from them, and that this haphazard arrangement was founded upon the application of federal principles of finance which have not been adopted in any other federal Government in the world.*

* Dr. Ambedkar holds that the system of divided heads of revenue is not in itself objectionable and that it does not necessarily imply interference by the Central Government with the spending powers of the provinces. It may work quite satisfactorily if exclusive assessment of a particular source of revenue by one tax jurisdiction is coupled with an apportionment of a part of the proceeds to another tax jurisdiction. See Ambedkar: *Provincial Finance*, p. 253.

According to the same body the origin of the whole trouble was in the academic insistence by the framers of the Montagu-Chelmsford Report on the theory of complete federal separation. The history of federal and provincial finance elsewhere shows that an absolutely clean cut between the Central and Provincial revenues is not possible.

The abolition of the contributions has aggravated provincial inequalities. The agricultural provinces like Madras find themselves in possession of substantial revenues which the land gives them. The industrial provinces, deprived of income tax, their principal source of growing revenue,* are unable to finance the nation-building activities. "Compared with the revenue in 1912-13, the agricultural provinces of the Punjab and Madras have increased their revenues by 162 per cent and 117 per cent respectively. The increase in the industrial provinces of Bengal and Bombay is only 63 per cent and 81 per cent respectively. Since the introduction of the Reforms, the revenue of Madras has grown by 522 lakhs and that of the Punjab by 563 lakhs. Bombay's revenue has increased by 263 lakhs and Bengal's revenue by 261 lakhs. In other words, the two major agricultural provinces are enjoying twice the enhancement of income secured by the two major industrial provinces."† Although the agricultural provinces are at present in a comparatively happier position, there is no doubt that in course of time they will also become restless as their activities expand and their essentially inelastic revenue sources refuse to expand proportionately.

There will thus be no peace until the whole system is radically overhauled in favour of the Provinces and the problem deliberately faced for what it is, viz., a problem in federal finance to be solved according to certain well recognised principles.¶

* Pretext against the deprivation led to a minor change in the system, by which, for every rupee of income assessed over and above the income assessed in 1920-21, the Provincial Government receives three pies. But in practice this has meant no benefit to the Provinces as the amount of income assessed has not risen since 1920-21, and the Provinces receive no advantage from any increase in the rate of the tax or any share in the Super-Tax.

† Times of India, January 11, 1929.

¶ This question was discussed in several interesting papers read before The Indian Economic Conference, January, 1929.

The Simon Commission has been receiving a good deal of evidence on this matter.

§ 29. Statistics of Provincial Finance:—As illustrative of the present financial position of the Provinces and the nature of their responsibilities, we give the following figures relating to the Province of Bombay.

* *Chief items of Revenue and Expenditure of the Government of Bombay in 1921-22 and 1928-29.* (In lakhs of rupees.)

Revenue	1921-22	1928-29	Expenditure	1921-22	1928-29
Land Revenue	5,47	5,38	Direct Demands on Revenue	2,55	1,71
Excise	3,43	3,91	Irrigation	1,23	1,11
Stamps	1,64	1,70	General Administration	1,23	2,23
Forest (net)	75	74	Administration of Justice	71	74
Registration	13	12	Police	1,92	1,70
Irrigation (net)	36	55	Education	1,73	2,09
Receipts by Civil Departments	36	80	Medical	46	54
Civil works	21	18	Civil works	1,88	1,25
			Public health	29	30
			Agriculture	30	29

LOCAL FINANCE.

§ 30. Provincial Rates:—At one time Provincial Rates or surcharges on land used to be an important item in the budget of the Central Government. Today, however, they form a substantial part of the revenues of District and Local Boards. They were originally started in Bombay and Madras between 1865 and 1869 and were levied on land chiefly for the construction and repairs of roads, the upkeep of schools and dispensaries, village sanitation and other local expenditure. The principle was extended in pursuance of Lord Mayo's scheme of financial decentralisation. In 1871 Acts were passed levying similar cesses in Bengal, U.P.,

* See Budget of the Government of Bombay for 1928-29, Statements II & III.

Budget of the Bombay Government for 1928-29.

(In thousands of Rupees)

<i>Revenue :</i>		<i>Expenditure :</i>	
Principal Heads of Revenue:—		Direct Demands on	
Taxes on Income	...	Revenue	1,71,66
Land Revenue	5,38 00	Revenue Account of Irrigation, Navigation etc.	1,00,80
Excise	3,91,18	Capital Account of Irrigation, etc. (charged to Revenue)	10,00
Stamps	1,70,10		
Forest	73,94		
Registration	11,94		
Scheduled taxes	21,37		
		<i>Debt Services:—</i>	
Total ...	12,06,53	Interest (a) Ordinary	98,46
Irrigation, Navigation etc., for which capital accounts are kept (Net receipts)	54,12	(b) Development	1,09,36
" " for which no capital accounts are kept	85	Reduction or avoidance of debt (a) Ordinary,	6,53
<i>Debt Services:</i>		(b) Development,	7,90
Interest (a) Ordinary	1,02,62		
(b) Development	48,04	Total ...	2,22,25
		<i>Civil Administration:—</i>	
Total ...	1,50,66	General Administration	2,23,33
Receipts by Civil Departments	80,49	Police	1,70,27
Civil works	17,72	Education	2,09,26
Bombay Development Scheme	21,25	Other Departments	2,19,43
Total ...	38,97	Total ...	8,22,29
Miscellaneous	41,73	<i>Civil Works:—</i>	
Provincial contributions and miscellaneous adjustments between Central & Provincial Govts. ...		Civil Works	1,24,97
Extraordinary items	23	Bombay Development Scheme	26,23
Total Revenue ...*	15,73,58	Total ...	1,51,20
Deficit	† 76,25	Miscellaneous	96,65
Grand Total ...	16,49,83	Contribution and Assignment to the Central Government by the Provincial Government	37,27
		Extraordinary Items	...
		Total Expenditure charged to Revenue	\$16,49,83

* Ordinary 15,25,54

Development 48,04

† Ordinary 34,53

Development 41,72

\$ Ordinary 15,60,07

Development 89,76

and the Punjab. In the Punjab and Oudh, cesses for roads, schools and the District Post, assessed at the time of the land revenue settlement were continued side by side with the new general cess. Similar settlement cesses were introduced in the Central Provinces, Burma and Assam, which were later replaced by a general cess. Between 1871 and 1905, there were added certain cesses for Imperial purposes. The Famine Insurance Fund was instituted in 1878, to which were added, in some provinces, cesses for provincial purposes, chiefly for the payment of village officers. The financial improvement in the position of the Government of India made possible the abolition in 1905-06 of all cesses levied for other than local purposes. In some cases, however, the effect of this reform was not to reduce the amount of the cesses levied, but to transfer the fund from provincial to local purposes, the Provincial Government being compensated from the Imperial Treasury. Recently there has been a tendency in some Provinces like Madras to add new cesses for specific local purposes such as elementary education. The basis of these local cesses on land varies with the system of land revenue. Thus in the Rayatwari areas of Bombay, Madras and Burma, the Central Provinces and Berar and in the temporarily settled areas of Assam, the cess is levied on the basis of land revenue. In the United Provinces and the Punjab on the other hand the annual value is taken at twice the land revenue as the basis. In the permanently settled areas either the rental value or the acreage is accepted as the basis. As regards the rates of the cesses they are left to the discretion of the local bodies subject to certain maxima and minima laid down by the Provincial Legislatures. The land cesses are collected along with the land revenue but are largely administered by the Local Bodies. The limits vary from $6\frac{1}{2}$ per cent to $12\frac{1}{2}$ per cent. The land cess, although it is not proportioned to ability to pay being levied at a flat rate, is everywhere recognised as an appropriate tax being applied for the benefit of the properties which again by the activities of the Local Boards. We have already referred to the recommendations of the Taxation Enquiry Committee that the land revenue should be standardised at a low rate so as to leave a wider margin for local taxation.*

* See Vol. I Chapter XII.

§ 31. Inadequate Resources of Local Bodies:—With the inauguration of the Reforms and the transfer of Local Government to the Ministers, the question of local finance has come into increased prominence. Considering the importance and wide range of functions assigned to the Municipalities, Rural Boards and Panchayats, such as public health, education, etc., the resources of these bodies are at present so scanty and inadequate that it is impossible for them to introduce modern standards of administration unless they are put on an ampler financial basis. Under the new constitution the Local Bodies are called upon to meet expenditure on services previously rendered gratis by Government servants belonging to the various departments. Also, in the first flush of enthusiasm the Local Bodies forgot that “all undertakings depend upon finance”* and launched costly and ambitious schemes of education, medical relief, etc. which were beyond their powers. The financial difficulties thus caused have recently been met partly by retrenchment, partly by additional taxation and partly also by a more careful distribution of the available resources.

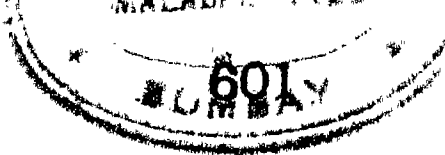
§ 32. Municipal Finance:—The main source of the income of municipalities is rates and taxes which account for about two-thirds of the total municipal revenues. The remaining one-third is derived from municipal property, contributions out of provincial revenues and miscellaneous sources. The taxes levied by the local authorities may be grouped under four heads:—
(1) Taxes on trade e. g., octroi duties, terminal taxes, tolls, etc.,
(2) taxes on property e. g. taxes on houses and their sites (and in rural areas the cess on land); (3) taxes on persons e. g. taxes on circumstances, professions, trades and callings, on pilgrims, on menials and domestic servants, etc.; and (4) fees and licenses. Fees are either for specific services rendered by the municipality such as scavenging fees or are partly of the nature of luxury taxes and partly levied for purposes of regulation such as licenses for music, vehicles, dogs and other animals etc. There are also license fees for offensive and dangerous trades. The Taxation Enquiry Committee point out that

*Kautilya's dictum adopted as a motto by the Taxation Enquiry Committee.

considerable vigilance is necessary in respect of indirect taxes, such as taxes on trade taking the form of octroi, terminal taxes and tolls, so as to prevent undue interference with inter-provincial traffic. Special objection is taken to the octroi and terminal taxes which offend against all the canons of taxation, and substitutes such as a tax on retail sales or profession taxes are suggested. At any rate a judicious modification of the present system of octroi duties is necessary. Another important suggestion of the Committee is in favour of increased assessment of town property which benefits largely from Municipal activities. The machinery for collection and assessment, however, would have to be far more efficient for this purpose than it happens to be to-day. The heaviest items of expenditure are conservancy and public works, each of which accounted for about 15 p. c. of the total expenditure in 1922-23. Water supply accounted for 14 p. c., drainage 6 p. c., and education only 8 p. c. The municipalities are often unable to meet their expenditure from ordinary revenues and have generally therefore to borrow money either from Government or in the open market to carry out such large projects as water supply, drainage works etc. The borrowings of the Bombay Municipality are the biggest amounting to 20 crores of rupees.

§ 33. Local Boards:—Provincial Rates constitute the most important item of the income of Local Boards, representing a proportion to total income varying from 25 p. c. in Bombay to 63 p. c. in Bihar and Orissa (in 1922-23). We have already indicated the origin of the local cesses on land, the basis on which they are calculated and the rates at which they are levied. Recently in some Provinces there has been a tendency either to increase the general rate or, as stated above, to levy specially earmarked cesses for purposes like elementary education. Other sources of revenue are Government grants, cattle pounds, ferries, road tolls etc. The principal objects of expenditure are education (which has been asserting its claims more and more in recent years), medical relief and civil works such as roads and bridges.

§ 34. Causes of inadequacy of resources:—Apart from the general low taxable capacity of the people and their alleged un-



willingness to tax themselves for local purposes, other important factors explaining the inadequacy of local resources are the unfair distribution of revenues between the central, provincial and local authorities. In England the bulk of the contribution from land goes to the local bodies, the Central Government receiving only a very small amount as land tax. One of the reasons for the financial weakness of the local bodies in India is that the local bodies have developed by the process of devolution of powers instead of the process of a federation of strong, semi-independent smaller units into larger political units. Another reason is that the jurisdictions of the local bodies are usually so extensive as to remove them from effective touch with the taxpayers. Had it not been for this, the imposition of taxes on houses and persons by local bodies in the villages would have been easier. From this point of view, the restoration of the influence of the village Panchayats and a limitation of the functions of the bodies at present operating would be desirable.

§ 33. Improvement of resources:-Though the recommendations of the Decentralization Commission and the introduction of the Reforms have led to considerable financial freedom being conferred upon local authorities, there has been no material change, so far as the nature of the taxes imposed is concerned, except that the taxes which may be levied without the sanction of the Government of India have been specified in the Scheduled Taxes Rules.* The Taxation Enquiry Committee make the following recommendations with a view to increasing the resources of the local bodies: (a) Conversion of the *thathameda*,† the capitation tax and the *chowkidari* into sources of local revenue; (b) standardisation of the land revenue § at a low rate so as to give better scope for local taxa-

*The Scheduled Taxes which the local authorities can impose under these rules are tolls; taxes on land and land values; taxes on buildings; on vehicles or boats; on animals; menials and domestic servants; octroi duties and termianl taxes; taxes on goods imported into or exported from a local area; taxes on trades, professions and callings; taxes on private markets, taxes for services rendered, e. g. water rate and drainage tax; and fees for the use of markets and other public conveniences.

† General tax on land in Burma.

§ See also Vol. I, pp. 554-555.

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tion; (c) transfer to local bodies of a share of the collection of Provincial Governments from ground rents in towns and from an increase in the rates on non-agricultural land; (d) empowering municipalities to tax advertisements; (e) extending the scope of taxes on entertainment and betting, and giving local bodies a substantial share of the proceeds; (f) extending and improving the administration of the taxes on circumstances, property and professions; (g) reducing the import duty on motor cars and enabling the Provincial Governments to levy a provincial tax in lieu of tolls for distribution to local bodies; (h) empowering local bodies in selected areas to levy a fee for the registration of marriages; and (i) supplementing the resources of local authorities by subsidies which should be ordinarily restricted to services of national importance and granted in such a way as to enable the Provincial Government effectively to enforce efficiency.* Another way of increasing the resources of the local bodies is to extend the scope of Municipal trading and enterprise so as to lessen the existing dependence on taxes. In view of the comparative inelasticity of the local taxes it is desirable to make use of non-taxation sources to a larger extent than at present. In western countries, particularly in Prussia, the scope of municipal domain-landed estates and especially industrial and trading domain-is on the increase and there are municipal tramways, water-works, gas and electric works, burial grounds, bathing establishments, fisheries, docks, bakeries, theatres, inns and restaurants, mills, factories, dairies, etc.. All these enterprises are apparently not only rendering effective service to the civic population but are also a substantial source of revenue for the Municipalities.† This aspect of local finance has been entirely neglected in India and it appears worth while that the local bodies should explore its possibilities so as to add to their slender resources and increase the amenities of civic life.

* Taxation Enquiry Committee's Report, paras, 194-96.

† K. T. Shah and Bahadurji : *Functions and Finance of Indian Municipalities*, p. 434.

CHAPTER XIII

UNEMPLOYMENT.

§ 1. Scope of the chapter:—A permanent margin of unemployment among industrial workers is a feature of the economic system called into existence by the Industrial Revolution in the Western countries. Certain palliatives such as unemployment insurance allowances and poor relief funds have come into use more or less in these countries, without however touching the fundamental cause of unemployment, viz, a maladjustment between production and consumption inseparable from the existing individualistic system of competitive production for world markets. The post-war depression in industry has created an unemployment situation of unprecedented magnitude. But though the evil has manifested itself on a scale unknown in the past, the phenomenon of industrial unemployment itself is sufficiently familiar in the west.

With us here in India, the problem of unemployment presents aspects which, while equally difficult to tackle, are somewhat different from those in Western countries. In the first place, the vast majority of the population depends upon agriculture, and we have already seen* that, in most parts of India, there is seasonal unemployment in agriculture, for five to nine months in the year during the slack season, and discussed the question of suitable supplementary industries to keep the cultivator occupied during this period of enforced idleness. But a more serious aspect of the unemployment problem presents itself in connection with the periodical occurrence of scarcity or famine due to a partial or total failure of the monsoon leading to a partial or complete stoppage of agricultural operations over wide areas disengaging a vast quantity of agricultural labour and labour employed in industries subsidiary to agriculture. This is by far the most serious form of unemployment to which India is liable.

* See Vol I pp 295-96 above.

Turning to occupations and industries other than agriculture, we may distinguish between the manual or hard-handed workers and the intellectual and clerical or soft-handed workers constituting the so-called educated middle class. Regarding the former category of industrial workers, it is clear that unemployment among them, though not unknown, does not as yet exist on the Western scale for the simple reason that our industrial development is yet in its infancy. So far as we have any modern industries at all, they have been caught up in the world-wide depression and there exists at the present moment a certain amount of industrial unemployment in India also. Owing to the closure of workshops and factories, or retrenchment in them, a number of operatives, skilled and unskilled, are without work. But in more normal times, as we have already seen, the complaint is rather that there is scarcity of industrial labour than that there is unemployment among its ranks. Moreover, unemployment when it does come has not the same terrors for the operatives in India as in the West owing to the fact that most of our industrial labour has predominant agricultural interests. Often indeed work in a factory is regarded as a second string to the bow and taken up only during the slack agricultural season.

As distinguished from unemployment among industrial workers in organised industries, there is some unemployment among cottage workers. In our Chapter on the Economic Transition in India* and our discussion of the position of her cottage industries†, a general idea has already been obtained as to the manner in which the different classes of artisans have been affected by the transition and we have formed some notion of the hardship and distress which have been the portion of many of them, who, having lost their old occupations, have not found a satisfactory substitute for them.

Another species of unemployment which is comparatively a modern growth in India is middle class unemployment, affecting those who have attained a certain standard of

* Vol I. Ch. V.

† Vol II, ch III, pp. 91-106.

education and who depend more or less exclusively upon non-manual or clerical occupations. This is a problem that has recently pushed itself very much to the forefront.

In this chapter we propose to concentrate attention on (I) Rural Unemployment due to Famines* and (II) Middle Class Unemployment.

(I) Rural Unemployment : Famines and Famine Relief.

§ 2. Responsibility for Famines :—The frequent occurrence of famines in the last quarter of the 19th century accompanied by a political awakening of the people gave these calamities a prominence which possibly they would not have attained otherwise. Indian publicists attributed their severity to the industrial, financial and land revenue policy of Government. By the great majority of people, the British Government came to be regarded as the sole cause of famines and this facile view of things was not disturbed by unimpeachable historical evidence of equally, if not more, severe famines in the pre-British days. This uncritical attitude elicited the cheap retort that famines were entirely due to failure of rains—a circumstance beyond the control of the British or any other Government. This however rather missed the point of the critics who blamed Government not for withholding rain but for causing the impoverishment of the people which made them incapable of resisting the effects of occasional scarcity. In this chapter, however, we are not concerned with locating the responsibility for Indian poverty but with the less contentious subject of the nature of Indian famines and the machinery devised to combat them.

§ 3. Economic effects of famines :—The economic effects of famines are bound to be disastrous in a preponderantly agricultural country like India. The heavy mortality due to sheer starvation which used to be a regular feature of the famines in the old days has ceased to characterise modern famines; though the epidemics which still follow in the wake of

* We had first intended to treat ' famines ' under Agriculture, but on second thoughts, it appeared more logical to class ' famines ' along with other forms of unemployment.

famines send up the mortality figures very greatly. There is a general lowering of the efficiency of the surviving people and the suspension of cultivation involves a great economic loss to the cultivators. Food famines are often accompanied by fodder famines and the resulting loss of cattle further hampers agriculture. There is also an adverse reaction on trade and industry due to the loss or reduction of the purchasing power of large numbers of people. Public finance is greatly disorganised and government is hit hard both on the side of revenue which inevitably shrinks and of expenditure which equally inevitably expands.

§ 4. History of famine relief.†— The history of famines and famine relief in India can be briefly told. It is wrong to suppose that in the pre-British days there were no famines at all or that they were less severe than in the present days. We read that in the famine of 1291 whole families drowned themselves as an escape from starvation, also that in the famine of 1555 people tried to live on the hides of dead beasts, and that the famine of 1630 actually led to cannibalism. In the face of these terrible records of well-authenticated facts it is impossible to subscribe to the popular opinion that the British in some mysterious way brought famines with them to India. Famines on the contrary were more common in pre-British days while, owing to defective communications, the system of famine relief was unavoidably less effective than at present. There were central granaries at the capitals which were originally maintained as war chests, but which in times of famines could be used to feed the starving poor. As communications were undeveloped, the village rather than the central government became the vital organisation of society and it was the surplus grain stored in the villages from which any relief could be expected. The efficacy of this arrangement depended on the intensity of the famine and its duration. The construction of public works like canals and tanks or the erection of temples, mosques, forts or palaces at public expense gave employment to a number of people and may have been useful in mitigating distress. Lastly, it may be believed that the

† For a brief but excellent treatment of famines in India see Loveday: *History and Economics of Indian Famines*.

kings occasionally attempted direct charity, which, however, from the nature of things could not have been anything but inadequate as a remedial measure.

Coming to the British period, the most important famines during the regime of the East India Company between 1760 and 1857 were those of 1770, 1784, 1802, 1824 and 1837. Excepting the first in the list, these famines did not receive the same elaborate attention, either at the hands of the Government or of the historians, as the famines of the latter half of the 19th century. The minds of people were preoccupied with other grave matters such as the continuous wars, the widespread disorder caused by the sudden introduction of unfamiliar judicial and land revenue systems and a corrupt administration in the hands of ill-paid and inexperienced officials, unemployment on a large scale caused by the sudden demobilisation of the troops of Indian princes, the depredations of the pinadaris etc. The political and administrative preoccupations of the Company made it indifferent to the question of the economic regeneration of the people. Even if it had the opportunities, it is doubtful whether it would have had the will to do anything, because its whole outlook was vitiated by commercial considerations and it seemed to be more concerned with the dividends of its shareholders than with the lives of those from whom these dividends were drawn. The Company in the later years of its existence acknowledged in a general way its obligations to the famine-stricken people; but it did not evolve any systematic famine policy. Slipshod and spasmodic efforts were made to deal with famines by regulating prices and trade in corn, encouraging emigration and occasionally undertaking public works. But all this was merely playing with a vast problem.

It is to the period following the transfer of India to the Crown in 1858 that we must turn for the elaboration of a proper system of prevention, insurance and relief evolved through many experiments and failures. In this period fall several great famines such as that of North-West India in 1860, of Orissa in 1865, of Rajputana in 1868, of Bihar in 1873, of South India in 1876 and the two widespread famines of 1896 and 1899-1900

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which affected various parts of India including Bombay, Madras and Central Provinces. The Orissa famine of 1865 affected five crores of people and was responsible for a heavy mortality of 10 lakhs. Government were slow to take action in the beginning, though food was later poured in large quantities into the affected areas. The great loss of life in this famine led to an inquiry presided over by Sir John Campbell and Government announced it as their definite policy to save life at any cost. In the Bihar famine of 1873 Government erred in the direction of indiscriminate charity and excessive expenditure. The great South India famine of 1876-78 involved a mortality of 52 lakhs. This led to the appointment of the first great Famine Commission presided over by Sir Richard Strachey, and on the measures taken by the Government of India at the instance of this Commission is based the subsequently elaborated machinery of famine relief. Among the steps taken by Government may be mentioned the introduction of a famine insurance grant in the annual budget, to be spent mainly on the construction of public works of a protective nature; the extension of communications by the system of the 'new guaranteed railways'; the clear definition of the principles of famine relief as provision of work to the able-bodied at a wage sufficient to secure health but not ordinary comforts and gratuitous relief to the infirm in their own villages or in poor houses; assistance to the land-owning classes by way of *tagavi* loans; and the suspension and remission of land revenue. Famine codes embodying these principles were made for every province. These codes were put to a severe test during the famines of 1896-97 and 1899-1900 and were amended in the light of the experience then gained. The earlier of these famines was followed by the appointment of a Commission presided over by Sir James Lyall, which made certain recommendations for the relief of special classes like weavers and hill tribes, proposed rules for the management of charitable funds, advocated a freer grant of gratuitous relief in villages, but disapproved of the extension of decentralised relief works. The second of these famines came too rapidly on the heels of the first to allow Government time to consider these recommendations. In 1900 the Maharaja of Jaipur

donated sixteen lakhs of rupees to constitute the nucleus of the Indian Peoples' Famine Trust. In 1901 the last Famine Commission under Sir Antony Macdonell emphasised the importance of "moral strategy" or "putting heart into the people," that is, assisting the people by loans and other means immediately danger is scented. The machinery suggested for the purpose included the prompt and liberal distribution of Tagavi, early suspension of land revenue, and a policy of 'prudent boldness' involving the preparation of a large and elastic plan of relief, constant vigilance and full enlistment of non-official help. The Commission further drew attention to the necessity of devising measures for tackling a fodder famine and of saving cattle. Lastly it recommended the starting of co-operative credit societies and the extension of state irrigation works of a protective character. The amended famine codes embodying these principles have well stood the test of subsequent famines such as that of U. P. of 1907, of Ahmednagar in 1912, and the far more serious scarcity of 1918 and 1920, and these visitations of nature may now be said to have been brought more effectively under human control than ever before in the history of India.

§ 5. Change in the Nature of Famines:—One main cause why this satisfactory result has been brought about is that the nature of famines has entirely changed. The special Commission of 1867 defined famine as "suffering from hunger on the part of large classes of population", but the history of famines in India is largely a discovery of a change in the meaning of that word brought about by two main factors: first, the improved means of communication and transport which have linked the various parts of the country into one single unit, so that deficiency in one part can be relieved by drawing upon the abundance in other parts; and secondly, the progressive perfection of the administrative organisation dealing with famines.* We have now no such a thing as a food famine, for although the rains may fail in one part it is very rarely that this is not balanced by an excep-

* See Loveday: op. cit.

tionally good monsoon somewhere else in the country, and thus taking the country as a whole, there is generally speaking the usual quantity of food available. Since modern famines are not food famines but money famines, what the state is called upon to do is to provide work and wages on an adequate scale. At present a famine is more accurately described as a temporary dislocation of employment due to the failure of crops, than as widespread death from starvation. Famine relief therefore primarily consists in providing employment for those against whom nature has declared a temporary lock-out.† When ordinary employment fails, Government opens relief works on which practically every one who seeks employment gets it and is able to earn enough by way of wages to enable him to buy just sufficient food.

§ 6. Classification of Causes and Remedies:—We can best understand the complex character of modern famines by trying to classify the causes of famines and the various kinds of remedial measures that have been proposed or adopted to meet them. The causes may roughly be divided into two kinds: (i) Immediate causes like drought or the after effects of drought which are directly responsible for distress and misery among the people; and (ii) remote but fundamental causes which have to do with the intense poverty of the people and their consequent inability to resist the slightest disturbance of the normal economic life. The first kind of causes can be met by the adoption of measures for the alleviation of distress or by making wise provision beforehand and remaining always in a state of preparedness to meet the calamity. Storage of grain and fodder and all insurance schemes are instances of previous preparedness. For dealing with the second kind of causes we must dig deep down into the fundamentals of the question of Indian poverty. The solution of this tremendous problem has to be approached from many sides and involves the adoption of an all-round intensive programme of economic regeneration.

§ 7. Direct causes and remedies:—The chief direct cause of famines being deficiency or total failure of rains, it would be

† See Morison : *Economic Transition in India*, p. 124.

clearly an advantage if the probable character of the coming monsoon could be foretold. The Meteorological Department keeps a regular record of the weather conditions prevailing in the different parts of the country. It is supposed that these data and especially a scientific study of the conditions prevailing in the upper strata of the air are capable of furnishing sufficient clues for making successful forecasts about the monsoon. Excessive rains and floods are also causes of famines but the damage due to these can generally be repaired with comparative ease. Locusts and other insect pests and the various kinds of fungi are also responsible for failure of crops. Government mycologists and other experts are engaged in fighting these causes. The precautionary measures against famine include the Famine Insurance Grant by which a sum of one crore and a half is provided in each year's budget and is spent on direct relief, if there is famine, and in constructing works mainly of a protective nature if the year is normal. The Government of India used to allot funds out of this grant to the different provinces according to their needs. But after the financial decentralisation that followed the Montagu-Chelmsford reforms, each province provides for its own famine insurance. Funds from the Indian Famine Trust are used to help the poor from the superior classes who cannot accept relief from Government in the ordinary way. For meeting famines when they actually occur, however, Government mainly rely on the relief organisation which was evolved in the latter half of the 19th century. The increasing efficacy of this organisation is attested by the comparative ease with which the people stood the strain of the severe famine conditions of 1918.

§ 8. Description of relief measures.*:—A brief description of this organisation will give the reader an idea of the elaborateness of the machinery and of the minute care with which it has been perfected. (i) Standing preparations are made on a large scale. Valuable information is gathered about climatic conditions, crops and prices, births and deaths; programmes of suitable relief works are kept ready and brought up to date; the country

* See Imperial Gazetteer of India, vol. III pp 477—481.

is mapped out into relief circles; and reserves of tools and plant are stocked. (ii) When rains fail, a careful lookout is kept for danger signals such as rise in prices, restlessness of the people, their aimless wandering, contraction of private charity, and increase in crime, especially petty thefts. (iii) Government then take preliminary action and declare their general policy as based on moral strategy. Meetings are called at which Government policy is explained to the people, non-official help is enlisted, suspension of revenue is declared, and loans for agricultural improvements are made. Village inspection begins and preliminary lists of helpless persons are prepared. (iv) Then follows the first stage of actual relief. Test works are opened and, if considerable labour is attracted to them, they are converted into relief works on the principles laid down in the famine codes. (v) The next stage commences from December. Central relief camps are organised and gratuitous relief is given to the infirm in the villages. Poor houses are opened in towns and village kitchens are run for the benefit of children. The distress reaches its climax in May when there is fear of an outbreak of cholera. (vi) The last stage begins with the advent of the rains. The large relief works are closed down and people are moved in batches to smaller relief works near their villages so as to prevent the spread of epidemics and to facilitate the restoration of normal agricultural conditions without needless delay. Local gratuitous relief is extended and liberal advances are made to cultivators for the purchase of cattle, ploughs and seed. When the principal autumn crop is ripe, the few remaining works are gradually closed down and gratuitous relief ceases. The famine is ordinarily at an end by the middle of October. All this time the medical staff is kept ready to deal with cholera and malaria which generally supervene when the rains break out.

§ 9. Ultimate causes and remedies:—The great poverty of the people is the ultimate cause of famines and throughout the book we have been busy considering one or other of the numerous features of Indian poverty, such as the excessive reliance of the population on agriculture—an industry dependent on an uncertain rainfall—the decay of old industries and the absence of new ones, and a peasantry steeped in indebted.

ness, living from hand to mouth, without any reserve to fall back upon in times of scarcity. The remedies for increasing the economic strength and staying power of the masses include a great variety of measures more easily suggested than carried out, such as raising the credit of the cultivator and his standard of living; construction of direct and indirect protective works like irrigation canals, roads and railways; encouragement of private enterprise in digging and repairing wells improvement in general administration-more especially land revenue administration with a reasonably light assessment and a sympathetically administered system of suspensions and remissions; a well-thought out and liberal forest policy; improvement of agriculture through the agency of the agricultural department, agricultural colleges, research institutes etc., the fullest utilisation of the Co-operative Movement, development of large-scale industries and encouragement to cottage industries etc.

(II) Middle Class Unemployment.

§ 10. The scope of the problem:--The terms 'educated' or 'middle class' are expressions in common use but difficult to define precisely. It is obvious, however, that the test of mere literary would exclude the illiterate manual labourer and the illiterate though shrewd business man or resourceful farmer. Also, having regard to the usual interpretation of the terms 'middle class,' it is clear that the wealthy Zamindars on the one hand, and unskilled labourers and petty ryots on the other, must be excluded. It is not easy, however, to draw the dividing line exactly between the educated and the uneducated, or between the middle class, and the higher and lower classes. The Madras and the Bombay Unemployment Enquiries include in the term educated middle class, such persons as are not well-to-do enough to dispense with earning their own living follow non-manual occupations and have received some form of secondary or higher education. The exclusion of those who have received only vernacular education is justified in the Bombay Enquiry on the ground that the problem of middle-class unemployment, as generally understood, chiefly affects persons ordinarily engaged in the larger cities, who by the

nature of their education and occupation are English knowing and that it is difficult to approach those who are chiefly engaged in *pedhis* and small trading concerns. The Punjab Unemployment Committee, on the other hand, understand by the term 'educated class' those who have at least completed the full vernacular or anglo-vernacular course.

§ 11. The seriousness and extent of middle class unemployment: Middle class unemployment has in recent years assumed alarming dimensions and attracted widespread public attention. Several Provinces in British India have investigated the question through special Committees and their example has been followed by important Native States like Travancore. In 1922 a Committee with Dr. Meek as its chairman was appointed in Bengal. Similarly in Madras, in pursuance of a Resolution in the Local Legislative Council, a Committee was appointed on 25th August 1925, with the Commissioner of Labour as chairman to investigate the question of unemployment among the educated middle classes. On 28th January, 1926, a Resolution was carried in the Assembly recommending the appointment of a Committee to investigate into the problem of unemployment, especially as it affected the middle classes. On 23rd September 1926, The Government of Bombay instructed the Director of Information and Labour Intelligence to hold an enquiry into middle class unemployment in the Bombay Presidency. The Labour Office in Bombay has accordingly carried out a statistical enquiry relating to Bombay City, Poona, Ahmedabad, Sholapur and other centres. On 16th February, 1927, the Punjab Government appointed a Committee to investigate into the extent of unemployment among the educated and uneducated classes of the community in the Punjab.

A perusal of these Reports leaves no doubt regarding the all-India character of the problem of unemployment among the middle classes. The Madras Committee point out that the proportion of educated men seeking employment to the demand for them is roughly two to one, and as the result of certain calculations about the annual output of schools and colleges and the proportion of vacancies occurring in the natural course of things, they

conclude that the amount of unemployment is very distressing. The Punjab Committee after similar calculations found that, whereas the output of Anglo-vernacular Schools and Colleges had more than doubled during the five years 1922-27, there has been nothing like a corresponding increase in the number of posts available in the Government Departments or in commercial and business firms. While the total number of applications received for a post which is advertised is by no means an accurate index of the extent of unemployment, for some of the applicants may be in possession of jobs and may yet desire to improve their prospects, it is nevertheless significant that two test advertisements in the Madras Presidency given at the instance of the Madras Committee called forth 666 and 787 applications respectively. The first was a clerk's post in the P. W. D. carrying a salary of Rs. 35 per mensem and the second was a clerk's post in a commercial firm on the same pay.

Unemployment on this scale is a more serious evil than is commonly recognised. Besides the individual suffering it causes to the unemployed, their disappointment and sense of injury produce a general demoralisation which is cumulative in its effect from generation to generation. The existence of a large number of disgruntled young men is also dangerous to the political stability of the state. The point has been well put by the Sadler Commission: 'The existence and the steady increase of a sort of intellectual proletariat, not without reasonable grievances, forms a menace to good government especially in a country where..... the small educated class is alone vocal. It must be an equal menace whatever form the government may assume. So long as the great mass of the nation's intelligent manhood is driven, in ever increasing numbers, along the same, often unfruitful course of study, which creates expectations that cannot be fulfilled, and actually unfits those who pursue it from undertaking many useful occupations necessary for the welfare of the country, any Government however it may be constituted, whether it be bureaucratic or popular, must find its work hampered by an unceasing stream of criticism and a

natural demand for relief which cannot possibly be met."* Again the gospel of revolutionary socialism or communism finds willing devotees in young men who nurse a strong sense of personal injury against a scheme of things in which apparently they have no place.

§ 12. Classes particularly affected:—The Bombay Enquiry makes it quite clear that, speaking of the unemployed in terms of age-groups, far and away numerically the most important section affected consists of young persons below 27 years of age.† Unemployment specially affects young men of the educated classes whose training has been purely literary and who have proceeded to higher education through the anglo-vernacular course. As might be expected, unemployment is most acute among those who have not succeeded in passing the School Leaving or Matriculation Examination which is considered to be the minimum qualification for Government service, less so among the S. L. C.s and Intermediates, and (comparatively) least of all among the graduates who possess no professional qualifications. The Bombay Report on the Enquiry into Middle Class Unemployment gives some interesting details regarding the educational qualifications of unemployed persons in the Presidency. " It is seen that 47.68 per cent of the total had not passed the Matriculation examination.....13.60 per cent of the unemployed had passed the Matriculation or an equivalent examination, 4.59 per cent were undergraduates, 7.02 per cent were graduates, 5.78 per cent knew typing, 1.73 per cent knew shorthand and the rest either possessed some other miscellaneous qualifications or specified them very imperfectly." (para 90). While there is great scope for the extension of education, as things stand, there is unemployment among teachers more among the untrained than

* Quoted by the Travancore Unemployment Committee's Report, para 79.

† 80.24 p. c. of the total unemployed persons were below the age of 32. 65.98 p. c. were below 27 years of age. The conclusion based on the figures for the individual centres, namely,‡ that unemployment is mainly restricted to the younger people, is also borne out by the combined results for the Presidency. *Enquiry into Middle Class Unemployment, Bombay*, para 85.

among trained teachers.* As regards the legal profession, it is commonly agreed that it is considerably overstocked and many junior members of the bar find it difficult to make a living. Similarly, the medical profession is overcrowded in the larger towns, though there is a paucity of medical men in the villages and smaller towns where the amenities of life are poor and the people not accustomed to pay regular cash fees for medical relief. There is much less unemployment among the engineers and the little that exists is tending to disappear with the relaxation of the policy of retrenchment and the starting of new public works. There are large numbers of persons who are fit and willing to be employed on the railways, but not yet trained, and therefore fail to get employment. As regards banking and accountancy, while those who have received advanced special training or acquired experience do not remain without jobs, there are scores of others who have had no special training and who fail to get employment.†

§ 13. Causes of Unemployment:--(i) *Post-war economic depression and retrenchment* :—India, like the rest of the world, has been affected by the post-war economic depression. Large numbers of persons employed in the clerical and the combatant branches of the army were discharged on the cessation of the War and it has not been possible to absorb them elsewhere, as even the normal volume of employment offered by Government and semi-public bodies and business firms has not been available. The axe of retrenchment has been applied in all directions and even the old establishments have not been fully maintained.

(ii) *Defects of the educational system*.—Another alleged cause of unemployment is the lack of adjustment between the system of education now in force in the country and the needs of industrial progress. The opinion is widely held that our present system of education is such as to produce persons qualified almost exclusively for the clerical occupation and is regarded

* Madras Report, pp. 6-7.

† Ibid. pp. 32-33.

merely as an avenue to Government service.* Sir George Anderson in his Note prepared for the Punjab Committee admits, that "in its very inception it (the present system of education) was moulded with the special object of preparing boys for external examinations, the passing of which is for many only a snare and a delusion, and with the object of training boys for clerical vocations which are now proclaimed to be overstocked and which offer insufficient avenues of employment to large throngs of applicants", and he proceeds to describe the Matriculate, whom he regards as the crux of the problem of unemployment, as "a derelict, a wanderer on the face of the earth, unemployed because he is unemployable." The average educated Indian looks first to Government service as a means of livelihood and, failing that, to clerical work under some official or semi-official body, such as railways, municipal and other local bodies, Port Trusts and the like. A further charge made against the educational system is that it renders boys unfit for their ancestral occupation, as they cannot for a minute picture themselves stooping so low as to earn their living with their hands and prefer being fifth-rate clerks after a smattering of education than earning a better income in the so-called manual occupations including agriculture.† The ranks of those who have traditional aversion to manual labour are thus swelled by the present system of education which is 'sterilising' and tends to "diminish the intellectual energy of those who receive it and is in many cases a positive disadvantage to them."‡ Parents belonging to the agricultural, artisan and backward classes are themselves becoming increasingly desirous of sending their children to schools and colleges with a view to Government service and the learned professions and thus fulfilling their cherished ambition of promoting themselves to the higher rungs of the social ladder. This

* "Our high schools and colleges suffer not for want of vocational training but for their concentration on training of a definitely vocational but very limited type. Essentially practical and utilitarian, they have aimed at the production of Government officials, lawyers, doctors, and commercial clerks." Mayhew: "*The Education of India*" p. 149

† Punjab Committee's Report. para 14.

‡ Sir Philip Hartog's Evidence before the Bengal committee.

fatal fascination exercised by the literary and quasi-literary occupations, within whose range of influence even the classes who have had no tradition of "letters" are being increasingly drawn, further emphasizes the prevailing unemployment among the educated classes.

We must, however, add that while it is true enough that parents do not display the necessary vision and foresight in choosing occupations for their boys, this may to a certain extent be attributed to the absence of suitable and adequate facilities for practical education—agricultural, technical, industrial or commercial.

(iii) *Social causes* :—There are also certain social causes such as the caste system, early marriage, the joint family system and communal inequalities, all of which "operate powerfully though silently in determining as well as impeding the economic ambitions and fortunes of the educated men."* For instance, caste fiat prevents educated men from taking to useful occupations which are regarded as undignified in the particular communities to which they belong. Early marriage not only interferes with adequate training for the work of life but also places too early in life the responsibility for maintaining a family on the shoulders of the young men. The Joint Family system, while it makes the burden of this responsibility lighter and offers protection to the weak and the helpless,† leads to economic parasitism and cramps individual initiative and ambition. Unwillingness to move out of their abodes and seek their fortunes away from their homes which is one of the results of the Joint Family system is another suggested cause of unemployment among the educated classes. But according to the Madras Report this immobility is on the decrease and has little bearing on the bulk of unemployment, which is mainly the result of the supply of men being far in excess of the demand for them.¶

* Madras Report p. 18; also See Vol. I, Ch. IV.

† The Bombay Report shows that 49.46 p. c. of the total or nearly half the unemployed persons in the Presidency were supported by their relatives during the period of unemployment, 8.15 p. c. maintained themselves on previous savings, 7.67 p. c. by casual work, 4.91 p. c. by income from real property. Cases in which the unemployed had to depend upon vicarious charity were comparatively few. Para 94.

¶ Madras Report, p 18 and p. 27.

(iv) *Economic backwardness*:—The most important cause of middle class unemployment is the very poor industrial development of the country and the paucity of openings available for educated young men. In England there are altogether about 16,000 occupations excluding Army, Navy and Civil Services. In India they are perhaps less than 40.* The mere extension of the facilities for vocational and technical training, it must be remembered, does not fully meet the situation. It will no doubt speed up the development of industries but it will not by itself call them into existence unless special measures are adopted simultaneously for the promotion of industries to absorb the trained men. In the usual discussions about the causes of unemployment, sometimes exaggerated emphasis is placed on the excessively literary character of the present system of education in this country and on the presence of caste prejudices, to the neglect of other factors such as the underdevelopment of the economic resources of India. This, as has been repeatedly pointed out, is at the basis of the poverty of the masses and in the last analysis dominates all species of unemployment.

§ 14. Remedies for Unemployment:—The causes of unemployment being many and various there can be no one sovereign remedy for it. In the first place, certain palliatives which have been put forward may be noticed. Employment Bureaux run by Universities, Government Departments or private agency have been suggested. These would undoubtedly serve a useful purpose if efficiently managed so as to secure public confidence. We must, however, remember that they can at the most bring about a better adjustment between supply and demand. They cannot provide any corrective to the tendency of the growing excess of supply of men in relation to the demand for them. §

Migration or emigration has also been proposed as an antidote to unemployment, but since middle class unemployment is an all-India problem, migration within the country can hardly be regarded as a solution. It can at best only transfer the unemployment problem from one place to another or from one

* See Travancore Report para 58.

§ See Madras Report, p 21.

province to another. As regards emigration we have already argued elsewhere* that, under the existing circumstances, not much relief can be expected from it. As stated above, unemployment of all grades and shades is in the final analysis the reflex action of economic backwardness and everything that leads to the economic betterment of the country will obviously be a remedy for unemployment. Material advance will not only create fresh avenues of employment for the middle class, but by raising the general level of prosperity attained by the community it will increase the demand for the services of lawyers, doctors, teachers etc. Further, with the increase in general prosperity coupled with the progressive Indianization of the superior civil and military services, the scope for employment in the administrative services will enlarge; and lastly we may add that any comprehensive programme launched by Government for bringing about the economic regeneration of the country will itself absorb immediately a certain number of the educated unemployed.

The Madras Committee declare that "the principal remedy (at any rate so far as Madras is concerned) for the present unemployment should be the diversion of the educated middle class, especially those who own or occupy land, to agriculture", and to facilitate this diversion, the Committee desire that "somehow or other the idea that the agriculturist is socially inferior to the clerk or lawyer, or the teacher, must be uprooted".¶ We have already had occasion to comment on the tendency towards absentee landlordism and the drift of the educated classes from the villages to the towns. These evils must be checked and the middle classes induced to apply their brains to agriculture and help themselves and the country. There are already signs that the prejudice against agriculture and other manual occupations is disappearing under the sheer weight of economic necessity.

The proposal of the Madras Committee to establish 'farm colonies' is of considerable interest but has its practical limitations. In the first place, barring provinces like

* See Vol I, ch III, pp. 102-103.

¶ Madras Report, para 25.

the Punjab, Assam and Burma, there is not much of good culturable land available for being granted to the educated unemployed, even if the superior claims of the village community and the depressed classes were to be ignored. Secondly, as the Madras Committee themselves admit, the temptation for the middle class parents to send their children to schools and colleges with a view to Government service would increase if it became generally known that Government would find land for the unemployed educated young men.

The Majority of the Punjab Unemployment Committee suggest that one way of relieving unemployment is that facilities for higher education should be provided only for the markedly able, who, if poor, should be subsidised by the state, or for those who can pay its full cost. (para 19). We do not think that anything should be done deliberately to increase the cost of education or to delimit the scope for higher education in the country, though we admit the necessity of somehow making parents realise that the present supply of men far exceeds the demand in government service and the legal profession, and that it is necessary for them to think of other careers for their children. There is more point in the suggestion of the Travancore Committee that the question of recruitment to all grades of government service by means of competitive examinations should be seriously considered. Definite competitive tests will weed out a large number of candidates and prevent the useless "dissipation of energy involved in running about to secure recommendations or to cultivate patronage." Those who fail in the competition will know that government service is out of the question for them and this will impel them to do something else instead of hanging about indefinitely on the mere off-chance of obtaining an appointment some time. This will also raise educational standards and enable the services to get better recruits. We have already suggested that even if we admit the principle communal representation in the services, it should be tempered by competitive recruitment.* The subject of the reform of the educational system itself has already been discussed.†

* See Travancore Report, paras 88-90

† See Vol I pp 275-276 and 394-396; also Vol II pp 24-30

Lastly, it must be noted that side by side with the improvement of the educational system there must also be a radical change in the social system and in the general outlook of the people. All obsolete ideas and practices which hamper economic (and political) progress must be fearlessly denounced, and sustained and strenuous efforts must be made to destroy them. For as the Sadler Commission wisely remark, "The education of a people is not given by schools and colleges alone. Other influences blend with theirs—the spirit and temper of the community which they serve, the power exerted over its thoughts and character by prevalent aspirations and beliefs, the tone of its family life, the rules and restraints imposed by its social organisation, the conditions under which its daily work for livelihood is done."

APPENDIX

Report of the Royal Commission on Agriculture.

1. Summary of recommendations and conclusions.

We have already referred to the appointment of the Royal Commission on Agriculture and its terms of reference.* The Report was signed on April 14, 1928, and was published in July, 1928. In this place we propose to give a short summary of the conclusions and recommendations of the Commission.

(1) *General* :—No substantial improvement in agriculture can be effected unless the cultivator has the will to achieve a better standard of living and the capacity, in terms of mental equipment and of physical health, to take advantage of the opportunities which science, wise laws and good administration may place at his disposal. Of all the factors making for prosperous agriculture by far the most important is the outlook of the peasant himself. As this is in the main determined by his environment, the improvement of village life in all directions is the first essential step in a comprehensive policy designed to promote the prosperity of the whole population and to enhance the national income at the source. The demand for a better life can be stimulated only by a deliberate and concerted effort to improve the general conditions of the countryside, and the responsibility for initiating the steps required to effect this improvement rests with the Government. What is required is an organised and sustained effort by all those Departments whose activities touch on the lives and the surroundings of the rural population. The sympathy, interest and active support of the general public are also essential.

(2) *Organisation of agricultural research* :—The basis of all agricultural progress is experiment. However efficient the organisation which is built up for demonstration and propaganda,

* See Vol. I pp. 396-97.

unless that organisation is based on the solid foundations provided by research, it is merely a house built on sand. An Imperial Research Council should be constituted, the primary function of which would be to promote, guide and coordinate agricultural research throughout India. It would be a body to which the Imperial and Provincial Departments of Agriculture could look for guidance (without being subjected to any administrative control) in all matters connected with research, and to which such research programmes as they might choose would be submitted for approval. It would also serve to link research work in India with that in other parts of the British Empire and in foreign countries. It would also act as a clearing house of information in regard to agricultural and veterinary matters. It would make arrangements for the training of research workers. It should be entrusted with a non-lapsing fund of Rs. 50 lakhs to which additions should be made from time to time as financial conditions permit. In addition to three whole-time members—the Chairman who should be an experienced administrator with a knowledge, if possible, of Indian conditions, a member for agriculture and a member for animal husbandry—the Council of Research should consist of thirty-six members, eight nominated by the Government of India, eighteen to represent the provincial agricultural and veterinary departments, three to represent the Indian Universities, two to represent the Indian Central Cotton Committee and the planting community respectively, and five to be nominated by the Council for the approval of the Government of India. A Provincial Research Committee should be established in each of the major provinces to work in close co-operation with the Central Research Council. A Central Jute Committee should be formed (on the lines of the Central Cotton Committee) to watch over all branches of the trade from the field to the factory.

(3) *Agricultural Improvement*:—Intensive surveys should be undertaken when some specific problem is to be solved. Soil erosion by floods should be prevented either by the afforestation of the ravine tracts or by the terracing of land and the construction of earth and stone embankments. A definite programme is neces-

sary in respect of the economy of farmyard manure, utilisation of oilseeds crops by the development of a local oil-crushing industry, investigation of the economics of the bone-crushing industry prior to the establishment of the industry on a large scale. The highly important work of distribution of improved seed will mainly fall on the agricultural department who should however utilise the co-operative agency for the purpose. An officer of the rank of a deputy director of agriculture should be in charge of the work of seed distribution and seed testing. Agricultural engineering should be reorganised under the control of a Senior Engineer under the Director of Agriculture. As regards improved implements the aim should be the evolution of a small number of types of implements and machinery suitable for a wide range of conditions and suitable also for mass production. The improvement of existing agricultural improvements and machinery offers a more promising field than the introduction of new types. However, the manufacture of new types in India should also be encouraged e. g. by railway concessions, and a careful investigation by the Tariff Board of the handicaps under which Indian manufacturers are labouring owing to the high protective duties levied upon imported steel and iron. Problems of cultivation in dry tracts should receive closer attention than in the past.

(4) *Subdivision and Fragmentation of holdings*:—In tackling the problem of subdivision and fragmentation great caution and the utmost possible consideration of the opinions and prejudices of the people affected are necessary. An element of compulsion may be inevitable but compulsion should not be regarded as dispensing with the need for the most scrupulous attention to the wishes of the people. It should be reserved till the latest possible stage of a proposed scheme for consolidation and may be applied to secure for the majority the advantages which an obstinate minority might otherwise withhold. The State should undertake propaganda work and difficulties should not be allowed to become an excuse for inactivity. State action in favour of consolidation should be taken in a gradual manner where it is introduced under a permissive Act. Special areas should be selected for notification under a permissive Act and full enquiry

should be made into the opinions of the right-holders before any measure of compulsion is introduced.

(5) *Demonstration and Propaganda*:--In a country where there is widespread illiteracy ocular demonstration is the best method of convincing the cultivating classes of the advantages of agricultural improvement when it is thoroughly tested on a Government experimental farm. Demonstration plots belonging to the cultivators themselves, cultivated under departmental control or direction, are preferable, though demonstration farms may be useful for certain special purposes involving industrial as well as agricultural operations e. g. maintaining a small plant for making white sugar or a high quality of *gur*. Other recommendations are short courses in particular subjects for cultivators on demonstration and seed farms, peripatetic demonstrations of improved implements, organisation of agricultural shows, and publicity in a form approved by the public including leaflets, cinema shows, lectures, and especially demonstration trains etc. Taluka Development Associations such as those in Bombay might be started with advantage by other Provinces to do propaganda work in favour of improved agriculture under the control of Divisional Boards of Agriculture. A far greater use than at present of the co-operative credit societies for propaganda work by the Agricultural Department, the appointment of a propaganda officer for each province attached to the office of the Director of Agriculture, are other recommendations.

(6) *Animal Husbandry*:--The deterioration of live stock may be arrested by a reduction in the number of plough cattle along with an increase in their efficiency, attention to all matters that would tend to decrease the number of bullocks required for cultivation and an effort to secure better treatment for dry cows and cows in calf. Feeding and breeding are the two most important factors in cattle improvement. The productivity of the grazing grounds may be increased by regulation of grazing lands by Panchayats or co-operative societies; allotment of definite areas to cattle-improvement societies; supply of water, where necessary, to grazing grounds; cutting and storage of grass; utilisation of silage; and cultivation of Egyptian clover (*berseem*); etc. As regards cattle-breeding, special efforts such as limiting the

issue of breeding bulls to selected districts with regular inspection and intensive breeding operations are necessary. To improve the present unsatisfactory condition of milk supply in the towns, municipal corporations should organise co-operative societies for the supply of milk and establish large dairy farms. To secure proper representation for animal husbandry, it is proposed that one of the members of the Council of Agricultural Research should be an eminent scientist well-versed in some branch or branches of animal husbandry.

(7) *Forests* :—The possibilities of fodder supplies from forests to be drawn upon in times of scarcity should be carefully examined. Grass cutting should be preferred to grazing. The possibilities of afforestation for increasing fuel supplies and the incidence of railway freight should be thoroughly examined. Development of forest industries is a matter of great importance to agriculturists, especially to those who live in the neighbourhood of forests, and to this end a forest utilisation officer should be appointed in each province. Deterioration of forests should be remedied either by natural or artificial regeneration. A reclassification of forest areas is proposed into a major division in charge of commercial forests; and a minor division in charge of minor forests; fuel plantations; village woodlands and waste lands; and the transfer of more or less wooded areas now under the control of the Forest Department to village management is suggested. Short courses at the Agricultural colleges should be instituted for all newly recruited forest officers to foster a closer touch between the Agricultural and Forest Departments.

(8) *Diseases of live stock and their control* :—The drastic methods adopted in Western countries for stamping out contagious diseases are declared to be unsuitable to Indian conditions owing to the prohibitive cost of compensation, inadequacy of veterinary staff and popular prejudices against destroying healthy animals. It is necessary therefore to devise measures for protecting the individual animal. The serum-simultaneous method is preferred to the 'serum-alone' method. No charge should be made for preventive inoculation. The provision of veterinary aid in India is totally inadequate and the Commission recommend the establishment in each district of

a central veterinary hospital with a number of dispensaries serving the subdivisions of the district. The staff attached to these dispensaries should be increased and men sent out to tour in the surrounding districts. A substantial increase of veterinary officers of all grades is necessary. Veterinary research work should be concentrated at the Muktesar Institute.

(9) *Irrigation*.—A periodic revision of the position in regard to the outstanding projects is suggested, and the construction of protective irrigation works from borrowed funds is approved. The formation of Irrigation Punchayats for the distribution of canal water, further investigation into the economics of tube wells, co-operative sinking and working of wells, inquiry into the causes of abandonment of old wells, encouragement of the extension of irrigation from small streams by means of power-driven pumps, formation of local irrigation committees on the analogy of local railway advisory committees, establishment of a Central Bureau of Information on irrigation matters, preparation of drainage maps, appointment of a Director of Agriculture for Sind with Karachi as his headquarters in view of the importance of the Sukkar Barrage Project, are other recommendations.

(10) *Communications and Marketing** :—The most hopeful solution of the cultivator's marketing difficulties seems to lie in the improvement of communications and the establishment of regulated markets on the Berar model as modified by the Bombay Legislation. † This system can be advantageously extended to other crops than cotton. The Government of India should undertake an investigation into the possibility of standardising weights and measures throughout India without undue interference with local custom. Co-operative sale societies are the most effective method of enabling the cultivator to secure an adequate premium for superior quality. The Agricultural Department should help such societies by the grading of produce. Market surveys are recommended as a preliminary to the formulation of an effective policy for the improvement of marketing. An expert market officer should be appointed to the staff of the

* See Vol. II, Chapter VI, p. 235 and pp. 538-546 above.

† See Vol. I, p. 306.

agricultural departments in all the major provinces. In view of the growing importance of Indian agricultural products in Europe, the Indian Trade Commissioner in London should be given the assistance of an officer with experience of agriculture and Co-operation in India.

(11) *Agricultural Finance* :—No usufructuary mortgage of agricultural land should be permitted by law unless provision is made for automatic redemption within a fixed period of years of which 20 should be the maximum. Local conditions should be the guiding consideration with regard to the desirability of extending the principle of statutory restriction on the alienation of land. Facilities offered by the Land Improvement Loans Act should be made known more widely to landholders. Part of the allotment under the same Act should be placed at the disposal of land mortgage banks where these are firmly established. The co-operative movement should receive all possible encouragement. An enquiry into the causes of the failure of the Usurious Loans Act is recommended. If the provisions of that Act could be fully utilised, this would go far to remove the worst evils of uncontrolled usury. The Punjab Moneylenders Bill and the British Moneylenders Act are commended as models to the consideration of Local Governments, who should also carefully consider the case for a simple Rural Insolvency Act. The Income Tax Department should periodically review the position of the money-lenders.

(12) *Co-operation* :—Every effort should be made in all provinces to build up a highly educated and well-trained official staff. The time has not yet come for the elimination of the official staff. The extension of the system of organisation of a supervising agency by federating primary societies into supervising unions is recommended. The personality of the Registrar is a matter of vital importance and the best man available should hold the post. Efforts in the direction of organising and developing Provincial Unions or Institutes deserve every encouragement, including grants-in-aid from Government, assistance by way of contributions towards the out-of-pocket expenses of honorary organisers, assisting institutions whose object is to spread education and the application of co-operative principles and promot-

ing specialised forms of co-operative activity such as consolidation of holdings, adult education, irrigation and the like. Regarding the question of land mortgage banks, the Commission endorse the resolution passed by the Conference of Registrars of 1926 in favour of the establishment of such banks under the provisions of the Co-operative Acts. Government should assist such banks by the guarantee of interest on debentures issued by them rather than by subscription to their debentures. Land mortgage banks would be a suitable agency for distribution of loans under the Land Improvement Loans Act. The debentures of such banks should be considered to be trustee securities. A central organisation is necessary to control the issue of such debentures. Otherwise the position will arise of a number of small institutions flooding the market with competing issues. Land mortgage banks should be organised after the most careful preliminary enquiry, and their constitution and working should be as simple as possible. For some years to come there should be an official member on the committee of management of each bank. The Commission prefer, as a matter of principle, the single purpose society to the multiple purpose society. Expert advice should be liberally given to ensure substantial progress in non-credit co-operation. Outside the credit movement, the main function of the co-operative departments is to prepare the ground for full utilisation of the advice of experts, employed by the Government in its several departments, organised for rural welfare.

(13) *The Villige*:—The Commission refer approvingly to the Madras District Health Scheme and the Bombay Village Aid Scheme and the scheme for subsidising medical practitioners to settle in small towns and villages. The improvement of water supply in villages is most important. To fight malaria, a much freer distribution of quinine is necessary and the Central Government should be responsible for the development of cinchona cultivation, the manufacture of quinine and control of distribution so far as the price within India is concerned. There is an urgent need for developing the rural medical and public health services to the utmost possible extent and with the utmost speed. The establishment of a Central Institute of Human Nutrition *

* See also Vol II, pp. 201-205.

is recommended. Villagers have ample time at their disposal for improving the amenities of the village by co-operative action under proper leadership and the institution of village guides for a group of villages trained on the lines adopted in the Gurgaon district of the Punjab is highly commended. Social workers organised into societies should be enlisted for linking village and town life. Every province should try to establish a Bureau of Rural Economic Research on the lines of the Board of Economic Enquiry in the Punjab. Careful attention is invited to the Punjab Central Rural Community Board which combines the advantages of both the official and private type of organisation. Co-operative Better Living Societies should be established. The question of co-operative arbitration for the settlement of village disputes should be carefully considered. Private organisations have a very inviting field for raising the members of the depressed classes in the village into full membership of the common life through education and inculcation of self-help.

(14) *Education*:—Compulsory primary education is the only remedy for the present unsatisfactory position. Co-operative education societies on the lines of those formed in the Punjab are recommended, and the importance of the proper choice and training of the teacher is stressed. While rural bias may be imparted to primary schools no attempt should be made to teach agriculture at this stage. Adult education is primarily a matter for non-official activity. Vernacular middle schools on the lines of the Punjab experiment, which include agriculture as an optional subject in the curriculum are recommended in preference to the Loni type of schools.* It is desirable to add to the curriculum of high schools in rural areas a course in agriculture. The Universities can make a valuable contribution to rural development, and agricultural colleges should be affiliated to them. Agricultural or rural economics should receive greater prominence in the agricultural college courses. A period of post-graduate training should be an essential qualification for direct recruitment in the higher grades of the agricultural service. An Agricultural College at Dacca and one for Bihar and Orissa are suggested.

† See Vol. I pp. 394-395.

Facilities should be provided to enable passed students to obtain further practical experience before commencing active work either in the public service or on their own lands.

(15) *Rural industries and labour*.—The multiplication of industries of the ordinary commercial type, such as cotton gins, rice mills and sugar refineries, supplies one solution of the problem of spare-time employment in rural areas. New industries such as implement firms should be established throughout the country, for which the staff should be trained by the Government. There are opportunities for the development of a poultry industry with Government assistance. An inquiry into the economics of the lac industry is recommended. The chief solution of the problems of the cultivator is intensification or diversification of his agriculture. Co-operative societies formed by village artisans should be encouraged by the Departments of Co-operation and Industries in each Province. Small factories will multiply with the progress made by the industrialisation of the country—a tendency which will be to the cultivator's advantage. The best chance for the smaller industries to hold their own is technical education and co-operative organisation. Government should advise and make suggestions for the development of small industries and make itself responsible for a new industry in its pioneer stage. To lessen the pressure of population on land, all restrictions on the internal migrations of labour should be abolished and definite schemes of colonisation, where possible, should be encouraged.

(16) *Horticulture and Plantations*.—The Commission hold that fruit growing can seldom be profitably combined with ordinary cultivation by the small cultivator owing to serious financial and other difficulties. Improvements in transport, picking and packing of fruit, as also suitable marketing arrangements are necessary. The prospects of market gardening (vegetables) are more hopeful than those of fruit culture. Much research work in connection with fruits and vegetables and an enquiry into their economic possibilities are desirable. The planting industries which deal principally with tea, coffee and rubber are well-organised and there should be co-operation between the Associations formed by these industries and the

Agricultural Department, and their joint representation on the Council of the Research Board is recommended.

(17) *Statistics*:—The Commission after reviewing the present position regarding statistics affecting the rural areas, make several useful recommendations for their modification and extension. They invite the co-operation of private individuals and associations working on a common plan under the aegis of University organisations or semi-official bodies of the type of the Punjab Board of Economic Enquiry to prosecute research into such sociological problems as indebtedness, mortgage debt and fragmentation of holdings. The objects of statistics collected by Government agency are declared to be the supply of information required by Government to discharge its functions and secondly, the supply of information required by the producers and the general public. Each agricultural department should be strengthened by the appointment of a statistical assistant and an expert statistician should be attached to the Imperial Agricultural Research Institute.

(18) *Agricultural services* :—The Commission make a number of recommendations for reorganising the agricultural services and defining the status, qualifications and pay of the grades of officers. They think that the field of recruitment to the superior provincial agricultural services should not be restricted to the province itself or to India in the interests of a wider outlook and variety of experience.

(19) *Miscellaneous* :—Recommendations are made in respect of a number of miscellaneous subjects, such as the agricultural development of the minor provinces, co-operation between British India and the Indian States, the establishment of a Local Self-government Institute as in Bombay, investigation of the problems of agricultural meteorology, the continued adherence of India to the International Institute of Agriculture at Rome (though the need for a special representative from India on its permanent Committee is not recognised by the Commission).

II Government action on the Report : The Simla Conference.

The Government of India in a circular letter dated July 23, 1928, to the various Provincial Governments suggested (a) firstly, that early action should be taken to examine the recommendations of the Commission and to classify them according to the order of urgency and financial feasibility; (b) secondly, that there should be a joint deliberation at a conference to determine the intrinsic value of the recommendations in order of priority and the line of action to be followed with regard to them; and (c) thirdly, that the Conference should endeavour to define the authority, central, or provincial, or both acting in unision, on which responsibility should rest. Accordingly, the Agricultural Conference consisting of provincial representatives (Ministers of Agriculture, Directors of Agriculture, Registrars of Co-operative Societies etc.) met at Simla from the 1st to 6th October, 1928. The main recommendations made by the Commission were discussed and action already taken by the various provinces in respect of some of the recommendations was ascertained, and emphasis was laid upon the financial implications of the Commission's proposals which made immediate or simultaneous adoption of them impossible. The Commission's Report was accepted as the basis for rural reconstruction and agricultural advance and for the progressive application of the main recommendations as the circumstances of each province might permit. The recommendations in regard to the Agricultural Services were to be left to the discretion of the Provincial Governments. The main recommendation regarding the Imperial Research Council to be set up and financed by the Central Government was approved of in general terms. *

III. Criticism and Appreciation.

In their seven hundred and odd recommendations the

* It is understood that Government have modified the organisation of the Council by splitting it into two, one to be called the Governing Body which will consist of about a dozen members including three members of the Central Legislature, and the other called the Advisory Body which will be composed mainly of experts. This is as it should be, for the Council as recommended by the Commission would be too unwieldy a body, and did not provide for any representatives from the Central Legislature.

Commission cover a very wide range of subjects. There is no straining after originality for its own sake noticeable in the Report. Consequently its conclusions are such as will command almost universal assent. On some subjects the recommendations are perhaps more halting and non-committal than they need have been. For example, on the question of subdivision and fragmentation, the Commission have adopted a "willing to wound but afraid to strike" sort of attitude. While recognising the seriousness of the evil, they stop short of definitely recommending the only remedy that has been found to be satisfactory elsewhere, viz., legislation with a certain degree of compulsion in it.

On the whole, however, the Commission are right in taking a conservative and practical view of rural and agricultural reform in a slow-moving country like India, and not recommending any swift and radical changes. This explains the commonest criticism of the Report that it contains nothing strikingly new. The complaint has been on the lips of many that the mountains have been in labour and brought forth a mouse. The Report, however, would have been a very curious, not to say, a dangerous document if it had studiously ignored everything that was old and already well established. So long as old truths are not being acted upon there is need and justification for every fresh repetition of them. There can be no question that the Report is a very valuable document and a rich storehouse of authoritative and up-to-date information on Indian rural conditions, and that as regard most of the problems it deals with, its recommendations and conclusions are helpful and enlightening. One of the undoubted benefits that may be confidently expected from the labours of the Commission is a general revival of interest in agriculture and a fuller realisation of its supreme importance to India. In the various educational institutions of the country, the pupils are likely in future to hear more about the problems of the countryside than they have been used to and the instruction imparted in the schools and colleges will bear a closer relation to the practical realities of life in India. There will take place a much-needed ruralization of urban thought and the most vocal sections of the community

will be vocal to better purpose, as they will have no longer any excuse for not knowing more about the actual conditions of life and labour in the rural areas. The Report has done useful service in recording in one place the measures already initiated in the different provinces for tackling problems of rural uplift. Hitherto the Provinces have generally been content to plough their lonely furrows without much of mutual help, knowledge or consultation. The Report should induce greater co-operation among them and a greater desire to learn from each other.

The fear has been expressed that the adoption of some of the recommendations will lead to a multiplication of posts carrying extravagant salaries and the importation of European experts who are no experts. However, since the need for research in agriculture is beyond dispute, the selection of a competent agency for taking charge of it is a matter which would require the utmost vigilance on the part of the Legislatures and the intelligent public. If they wake up betimes to the dangers of the situation, such as they are, it should not be impossible for them to prevent the apprehended abuse.

In order that any useful practical results should be reaped from the work of the Commission, each Province will have to undertake a special investigation into its own conditions in the light of the Commission's recommendations which are necessarily very general in character. Disappointment might also be avoided by not expecting too quick results. The process of implementing the recommendations of the Commission, which has just started, will inevitably be slow and difficult and all the resources of the Government and the community will have to be patiently mobilised for many years to come before rural India can hope to turn her back on the deep shadows and emerge smiling and prosperous into the radiant light of day.

Some select opinions on Vol. I.

The Servant of India:.....“the volume will be an indispensable *vade mecum* for all wishing either to gain or brush up their knowledge of economic problems in India. A large portion of the extant literature on the various subjects has been traversed and condensed wonderfully well so as to guide the reader instead of mystifying him. In the case of controversial questions both sides have been presented with fairness and impartiality although there is no attempt to burke definite pronouncements.....We are glad to find that the authors have made a clean sweep of the false prudery surrounding the discussion of the problems of birth-control and contraceptives.....On the whole the problem of population has been dealt with very fully and ably in the volume before us.....The chapter on the co-operative movement is one of the best in the volume and the treatment of the subject leaves nothing to be desired.....We heartily commend this volume to all students of Indian economic problems including publicists and workers engaged in active politics, who seek for a reliable presentation of these problems in their various aspects.”

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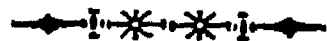
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(*We are indebted to Mr. N. A. Charankar B. A.
for the Index.*)

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